

WORKERS VS. SHAREHOLDERS UNDER UNITED STATES CORPORATE LAW: REFORMING CORPORATE FIDUCIARY LAW TO PROTECT WORKER INTERESTS

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INTRODUCTION

Despite both socio-economic and equitable reasons to consider workers'¹ interests in boardroom decision-making,² corporate boards have usually ignored such interests, and corporate law in the United States generally has not imposed a fiduciary duty on these boards to take account of those interests.³ Yet the social and economic consequences of corporate boards' lack of concern for workers' interests in the corporate decision-making process are dire.⁴ Between 1983 and 1988, 9.7 million employees lost their jobs due to layoffs and plant closings.⁵ In addition to losing their jobs, these displaced workers often also lose their health and pension benefits, deplete their savings, lose their homes to foreclosures, and must increasingly rely on public welfare.⁶ Nonetheless, corporate decision-making concerning such layoffs and plant closings has focused exclusively on shareholder interests while disregarding workers' interests.⁷ Extending fiduciary protections to workers, however, minimizes these social harms by ensuring that directors and managers consider the interests of workers in such decisions.

Sadly, conditions for employed workers are not much better. Regardless of increasingly high corporate profits, hourly wages for the bottom 80% of workers have

¹ The term "workers" includes working class employees who generally work for wages in low-skill manual, clerical, and retail positions, such as in construction, factory work, technical installation, data entry, or department store sales. Their jobs typically lack autonomy and supervisory responsibility and often do not require a college education.

² See *infra* notes 3-19 and accompanying text.

³ See *Revlon, Inc. v. MacAndrews Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986) (stating that "[t]he Revlon board argued that it acted in good faith in protecting the noteholders because *Unocal* permits consideration of other corporate constituencies. Although such considerations may be permissible, there are fundamental limitations upon that prerogative. A board may have regard for various constituencies in discharging its responsibilities, provided there are rationally related benefits accruing to the stockholders."); *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) ("[i]n carrying out their managerial roles, directors are charged with an unyielding fiduciary duty to the corporation and its shareholders."); *Dodge v. Ford Motor Co.*, 170 N.W. 668, 682 (Mich. 1919) (stating that "[t]here should be no confusion (of which there is evidence) of the duties which Mr. Ford conceives that he and the stockholders owe to the general public and the duties which in law he and his codirectors [sic] owe to protesting, minority stockholders. A business corporation is organized and carried on primarily for the profit of the stockholders.").

⁴ See Marleen A. O'Connor, *Restructuring the Corporation's Nexus of Contracts: Recognizing a Fiduciary Duty to Protect Displaced Workers*, 69 N.C. L. REV. 1189, 1192 (1991) (describing the results of substantial layoffs by Safeway Stores, Inc.).

⁵ *Id.* at 1197.

⁶ *Id.* at 1198.

⁷ See *id.* at 1199 (stating that "... recent corporate restructuring has brought about a sudden change in labor relations... currently, corporations seek to accelerate the timetable to reduce the workforce to the lowest possible level. In the process, many corporations display a diminishing regard for employees.").

fallen in the decade between 1990 and 2000.⁸ Even in the late 1990s, with a booming stock market, the richest 10% of the U.S. population received 85.8% of gains, while a typical American worker was working more hours for less pay.⁹ In fact, almost 30% of workers' wages are not high enough to raise them out of poverty.¹⁰ According to a US Census Bureau study, 18% of all workers in 1990 earned incomes so low that, despite fulltime employment, they placed a family of four below the poverty line.¹¹ The low quality of life these workers experience in contrast to the lucrative lifestyles enjoyed by their managers, supervisors, and corporate executives¹² has resulted in the highest level of income inequality since 1967,¹³ an increasing concentration of corporate income in the hands of capital owners, and a corresponding decrease in employees' share of corporate compensation.¹⁴

Additionally, there are numerous equitable reasons that warrant consideration of workers' interests in corporate decision-making.¹⁵ Workers make investments in human capital to the firm, justifying an integration of their concerns in corporate boardroom deliberation.¹⁶ While it is clear that workers who need to develop firm-specific skills make such an investment, a worker who merely contributes transferable skills such as basic time and labor has made such an investment as well.¹⁷ Moreover, employees form a reliance interest in their long-term employment relationship with companies.¹⁸ For

⁸ See Kent Greenfield, *There's a Forrest in Those Trees: Teaching About the Role of Corporations in Society* 5 (Boston College Law School, Public Law and Legal Theory, Research Paper No. 2000-01, 2000).

⁹ *Id.*

¹⁰ *Id.* at 6.

¹¹ See Joseph William Singer, *Jobs and Justice: Rethinking the Stakeholder Debate*, 43 U. TORONTO L.J. 475, 476 (1993).

¹² Greenfield, *supra* note 8, at 66 (stating that "[t]wenty years ago, pay for executive chief officers was less than 30 times that of the average worker. Now, the typical CEO makes over 400 times that of the average worker.").

¹³ Between 1967 and 2005, income for the lower limit of the highest household income quintile increased almost four times more than the increase in median household income during this period. See U.S. Census Bureau, "Income, Poverty, and Health Insurance Coverage in the United States: 2005" (August 2006), at <http://www.census.gov/hhes/www/income/reports.html> (indicating that median household income increased only about \$11,000 - from \$35,379 to \$46,326, and noting that the lower limit of the highest household income quintile in 2005 was \$91,705). Compare U.S. Census Bureau, "The Changing Shape of the Nation's Income Distribution: 1947-1998" (June 2000), at <http://www.census.gov/hhes/www/income/reports.html> (stating that the lower limit of the highest household income quintile in 1967 was \$53,170, reflecting an increase of almost \$40,000 for this income level between 1967 and 2005).

¹⁴ See Economic Policy Institute, "Economic Snapshots" (Jan. 17, 2007), available at <http://www.epi.org/content.cfm?id=2604> (last accessed April 2, 2007) (stating that "[t]he most recent data (third quarter of 2006) reveal that owners of capital received 23.0% of all corporate income, the highest since 1966. That means that the compensation of employees was at the lowest share in over 25 years.").

¹⁵ See Kent Greenfield, *The Place of Workers in Corporate Law*, 39 B.C. L. REV. 283, 283-287 (1998) (stating that "by any account, workers provide essential inputs to a corporation's productive activities, and... the success of the business enterprise quite often turns on the success of the relationship between the corporation and those who are employed by it... justifications for shareholder dominance - ownership, agency costs, the residual nature of their claims and inability to contract - are not as strong as generally proposed or often apply to workers as well.").

¹⁶ *Id.* at 289-300.

¹⁷ See *id.* (explaining a property basis for shareholders' rights).

¹⁸ See Joseph William Singer, *The Reliance Interest in Property*, 40 STAN. L. REV. 611, 724 (1988) (explaining this point).

example, when a plant closes, the laid off workers may face long-term unemployment or under-employment, loss of family wealth, and health and family problems.¹⁹ Consequently, if a company is considering closing a plant, it should consider the problems borne by the workers with whom it has established a long-term relationship.²⁰

The means available for workers to pursue their interests under the current legal regime are ineffective.²¹ First, it is argued that workers can contract with employers for specific protections, such as veto power over corporate acts.²² Workers, however, are unlikely to garner such contractual protections because employers often have no duty to negotiate over certain issues pertinent to workers, employers often have greater leverage in negotiations, and many contingent events affecting worker interests cannot be foreseen at the negotiation stage.²³ Moreover, the mere usurpation of fiduciary protections by shareholders causes workers to question the enforceability of employment contract terms and agreements between workers and management.²⁴ For example, a firm may want to defer a bonus to a worker until the firm's prospects improve or pay low wages now in exchange for higher wages later, but the worker will be reluctant to assent to such requests due to the belief that management's fiduciary duty to act in the best interests of shareholders compels management to use that extra money to further shareholder interests.²⁵ Thus, workers cannot effectively contract with management both because of their limited negotiating leverage and because shareholders' exclusive fiduciary rights may subject their contractual agreements with management to judicial scrutiny.²⁶

Second, it is argued that workers can protect their interests through employment and labor law rather than resort to corporate fiduciary obligations.²⁷ This argument, however, rests on the inaccurate assumption that corporate law should primarily concern itself with protecting the contractual relationship of constituencies rather than deal with normative concerns, such as the economic and societal consequences of its laws.²⁸ Moreover, because labor law is primarily concerned with regulating the union-employer relationship, and employment law generally addresses only every-day employment

¹⁹ *Id.*

²⁰ *Id.* at 724-25 (explaining the moral principles behind this idea).

²¹ See Jonathan R. Macey, *An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties*, 21 STETSON L. REV. 23, 36-38 (1991) (describing the fallbacks of nonshareholder constituency statutes).

²² See *id.* (describing the many assurances and rights that workers could potentially receive through contract negotiations).

²³ See Greenfield, *supra* note 15, at 313-21 (outlining the assumptions contractarian theory makes about a worker's ability to bargain during negotiations).

²⁴ See Oliver Hart, *An Economist's View of Fiduciary Duty*, 43 U. TORONTO L.J. 299, 306-7 (1993) (stating that "[m]anagement's promise not to renege is harder to sustain, however, if its fiduciary duty to shareholders is interpreted narrowly. The reason is that ex post, when management gives the worker his deferred compensation or gives the supplier a generous portion of the quasi-rents from the relationship, shareholders can sue, claiming that the money belongs to them. Anticipating this, of course, workers will not be prepared to undergo an apprenticeship or postpone compensation. . . .").

²⁵ *Id.* (giving bonus deferral as an example).

²⁶ *Id.*

²⁷ See Greenfield, *supra* note 15, at 283 (stating that "[t]he justification for insulating the concerns of workers from the attention of corporate law is that such concerns are the subject of other areas of law, most prominently labor law and employment law.").

²⁸ See KENT GREENFIELD, *THE FAILURE OF CORPORATE LAW: FUNDAMENTAL FLAWS, PROGRESSIVE POSSIBILITIES* 125-27, 153-55 (2007).

relations, these areas of law often do not address the most pressing issues for workers, such as plant closings.²⁹

Third, even if individual workers cannot garner the leverage to contract with employers, and even if employment and labor laws often do not address worker-related issues, unions can use their collective leverage to bargain for worker protections.³⁰ The effectiveness of unions to bargain for worker protections is mitigated, however, by a number of practical considerations and observations.³¹ First, only a small percentage of workers in the U.S. are represented by unions.³² Second, employers do not have the obligation to bargain with unions on many issues important to workers, such as plant closings.³³ Therefore, it is clear that although workers have a number of avenues through which to address their interests under the current regime, none adequately or effectively ensure the consideration of worker interests in making corporate decisions. As a method to address the current disregard for worker interests in corporate decision-making, this note proposes extending fiduciary duties to workers. An accurate understanding of fiduciary duties will reveal that this proposal is both practical and effective.

Part I of the note begins by examining why fiduciary duties have traditionally been limited only to shareholders and then criticizes the reasons for such a shareholder-dominance rule. This section demonstrates that the rationales commonly advanced in favor of restricting fiduciary duties are severely flawed.

Part II questions the feasibility of imposing a fiduciary obligation on corporate board members and managers to consider worker interests. Indeed, even if workers should be given these rights normatively due to their important status in the corporation and the ineffectiveness of current avenues to address their rights and interests, these rights must withstand the scrutiny of practical objections and obstacles.³⁴ The section will conclude that extension of fiduciary duties to workers can overcome obstacles because worker and shareholder interests often unite, because corporate law has always been able to reconcile competing interests, and because the inefficiencies critics warn of have not occurred in other countries who afford greater protections to labor.³⁵

²⁹ *Id.* at Ch. 3, p. 2.

³⁰ See O'Connor, *supra* note 4, at 1215 (explaining that "many commentators assume that unions will bargain to protect their members from the consequences of layoffs and plant closings.").

³¹ See *id.* at 1216-22 (discussing "the possible reasons why unionized employees have not sought contractual provisions to mitigate the consequences of restructuring").

³² *Id.* at 1215 (stating that "less than twenty percent of the work force is unionized.").

³³ See *id.* at 1216 (explaining that "Professor Stone describes the situations as follows: 'at the same time that corporate investment decisions are causing massive layoffs throughout the unionized sectors, the labor laws are being reinterpreted to give unions less and less input into corporate decision making.'").

³⁴ See Bernard Black, *Corporate Law and Residual Claimants* (Berkeley Program in Law and Economics, Working Paper Series 22, 1999), available at <http://repositories.cdlib.org/cgi/viewcontent.cgi?article=1045&context=blewp> (last accessed April 2, 2007) (discussing why residual claimants typically do not receive control rights and "why employees receive no formal control rights even though they are major residual claimants.").

³⁵ See Mitu Gulati, *Incorporating Labor*, 22 COMP. LAB. L. & POL'Y J. 171, 172 (2000) (referencing an article by O'Connor which points out that both Japanese and German corporate law systems "provide labor a far greater role than does the American system." The authors go on to state that "[g]iven the ability of corporations from these countries to compete on equal footing (and sometimes outcompete) their U.S. counterparts, this suggests that a greater governance role for labor will not bring with it all the inefficiencies that many in the United States often assume.").

Part III will consider both various mechanisms for extending fiduciary obligations to workers as well as alternative ways to address the problem of insufficient concern for workers in corporate decision-making without extending fiduciary duty rights to workers. This section concludes that the most practicable and effective method to ensure the integration of worker interests in corporate decision-making is to amend corporate law to impose on boards of directors procedural fiduciary duties owing to workers.

I. THE JUSTIFICATIONS FOR, AND CRITICISMS OF, THE SHAREHOLDER-DOMINANCE RULE
A. Fiduciary Duties Under Current U.S. Corporate Law

Under the current corporate regime, corporate board members and managers owe fiduciary duties only to the shareholders of a corporation rather than to other corporate constituencies or stakeholders.³⁶ Fiduciary duties in corporate law consist of directors' and managers' dual obligations to act with care and loyalty towards those to whom the obligation is owed, namely shareholders.³⁷ For example, these duties proscribe corporate acts that amount to self-dealing, uninformed decision-making, and ignoring the interests of those to whom a duty is owed in decision-making.³⁸ These legal duties give shareholders the right to sue board members or managers when these duties have allegedly been breached.³⁹

Although shareholders, as the sole beneficiaries of fiduciary protections, can hold directors and managers accountable for their decisions and thereby ensure consideration of their interests in boardroom deliberation, the fiduciary duties they are owed do not always guarantee good and honest corporate decision-making.⁴⁰ This is arguably due to the lax judicial review of management decisions under the business judgment rule⁴¹. Nevertheless, fiduciary duties owed to shareholders have theoretically granted them assurance that management will act in their best interest and have often provided shareholders redress and remedies in cases where management has not acted in the shareholders' best interest.⁴² Thus, despite the lax judicial review of management

³⁶ See *supra* note 3 and accompanying text.

³⁷ See *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) (discussing the obligation a director has to act with a duty of care "as distinguished from a duty of loyalty.").

³⁸ *Id.*

³⁹ See *Smith*, 488 A.2d at 864 (illustrating an example of a suit where plaintiffs sued because of this).

⁴⁰ See Marleen O'Connor, *Employees and Corporate Governance: Labor's Role in the American Corporate Governance Structure*, 22 COMP. LAB. L. & POL'Y J. 97, 107 (2000) (stating that "[F]iduciary law does not provide much protection to shareholders because courts are reluctant to second-guess business decisions under the business judgment rule. Even if workers have standing to sue to enforce such obligations, courts are likely to continue to shy away from engaging in substantive review of business decisions.").

⁴¹ See *id.*; See also *Aronson v. Lewis*, 473 A.2d 805, 812 (Del.1984) (indicating judicial reluctance to second-guess managers' business decisions and stating that "[i]t is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the decision to establish facts rebutting the presumption."); See also *Auerbach v. Bennett*, 47 N.Y.2d 619, 629 (N.Y. 1979) (explaining that "[t]hat doctrine bars judicial inquiry into actions of corporate directors taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes.").

⁴² See *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985) (describing a class action by corporate shareholders against board. The Court held that the board was liable to the shareholders because the board acted in a

decisions under the business judgment rule, the existence of fiduciary duties still offers those who are owed such duties otherwise unavailable protections.⁴³

Moreover, even if the business judgment rule's deference to corporate boards and managements would prevent workers from realistically obtaining relief from them, other considerations support extending directorial fiduciary protections to workers.⁴⁴ Legally recognizing workers' roles in corporate governance by extending fiduciary protections to them would foster improved labor-management relations,⁴⁵ because it would relay to managers and boards that they are partners in a common enterprise and thereby encourage cooperation and loyalty between the parties.⁴⁶ Also, as fiduciary law affords beneficiaries disclosure rights, workers would receive more information about corporate affairs that affect their investment in human capital.⁴⁷ Lastly, notwithstanding the business judgment rule's limitation on obtaining relief, the mere possibility of legal sanctions would at least serve as an additional incentive to management to consider worker interests and provide some assurance to workers that they can trust them.⁴⁸

Given the role of fiduciary duties in promoting honest, informed decision-making and imposing a method of corporate accountability,⁴⁹ it is questionable why these duties have only been owed to shareholders and not other groups of corporate stakeholders.⁵⁰ Indeed, the Committee on Corporate Laws, explaining the shareholder-dominant position of the Delaware Supreme Court in Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.,⁵¹ stated:

grossly negligent manner in approving amendments to a merger proposal and by failing to disclose material facts before securing the stockholders' approval of the merger).

⁴³ See *supra* notes 40-41 and accompanying text.

⁴⁴ See O'Connor, *supra* note 40, at 107 (concluding that "workers would benefit from recognizing a fiduciary duty in three ways... symbolic and pedagogic. . . . disclosure. . . . [and it would] encourage worker participation in strategic corporate decision making.").

⁴⁵ *Id.* (stating that "the most significant aspect of employment law is symbolic and pedagogic because, in many instances, the threat of formal sanctions is remote. Thus, legally recognizing the employee's role in corporate governance may promote greater labor-management cooperation.").

⁴⁶ See Marleen O'Connor, *The Human Capital Era: Reconceptualizing Corporate Law to Facilitate Labor-Management Cooperation*, 78 CORNELL L. REV. 899, 954-55 (1993) (explaining how this would work under her theory of fiduciary rights).

⁴⁷ See O'Connor, *supra* note 46, at 107.

⁴⁸ See O'Connor, *supra* note 46, at 955 ("[F]iduciary law would facilitate participatory work programs because the possibility of legal sanctions would provide some assurance to employees who are uncertain about whether to trust managers. Indeed, the very existence of judicial recourse for breach of fiduciary duty may deter opportunistic behavior by firms. By reducing the risks of trust, fiduciary law would provide support for cooperative corporate cultures by allowing employees to rely upon systems trust.").

⁴⁹ See WILLIAM A. KLEIN & JOHN C. COFFEE JR., *BUSINESS ORGANIZATION AND FINANCE: LEGAL AND ECONOMIC PRINCIPLES* 204 (Eighth ed., Foundation Press 2002) (1980) (stating that "fiduciary duties encourage thoughtful, honest decision-making by exposing corporate officers to the possibility of liability in a derivative action due to a fiduciary duty violation. Practically, although derivative actions' likelihood to deter fiduciary violations may be limited by shareholders' frequent difficulty in obtaining a recovery, they still produce a general deterrent benefit because "managers, both in the same corporation and in other corporations, might be deterred from future wrongful conduct by a few successful actions.").

⁵⁰ See Greenfield, *supra* note 15, at 287 (suggesting that "workers should have some kind of representation on the board of directors or have some role in electing directors, and that directors of companies should be held to have some kind of fiduciary duty to workers in the employ of their firm.").

⁵¹ See *Revlon, Inc. v. MacAndrews Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986).

Directors have fiduciary responsibilities to shareholders which, while allowing directors to give consideration to the interests of others, compel them to find some reasonable relationship to the long-term interests of shareholders when doing so. In Delaware, this principle is modified when the decision is made to sell the company, at which time the directors may consider only the interests of shareholders.⁵²

Moreover, even if non-shareholder constituencies' interests may at times be considered by management, the Delaware Supreme Court does not encourage the consideration of such interests.⁵³ Therefore, the reasons for not extending these fiduciary duties to workers must be both logically and normatively examined.⁵⁴

B. The Property-Based Justification for Shareholder Dominance

The traditional justification for shareholder dominance is that shareholders, through their contribution of capital and hiring of management,⁵⁵ are the owners of the corporation and thus the corporation is arranged primarily to serve them.⁵⁶ A variant of this argument is that shareholders' shares convey an ownership interest or property right in the firm that should not be limited.⁵⁷ As such, there should not be any consideration of non-shareholder constituencies because it would shift control from the "owners" and limit their property rights.⁵⁸

Both variations of the property-based justification for shareholder dominance mistakenly characterizes property rights as indivisible and unlimited.⁵⁹ Property rights are divisible in a number of ways, such as over time, through co-ownership, through leases, easements, covenants, and mortgages.⁶⁰ Thus, ownership of property does not necessarily equate with exclusive ownership of that property.⁶¹ As such, management can simultaneously take into account shareholder interests and worker interests as two different groups of owners of the corporation.⁶²

Also, property rights have always been limited by reasonable regulation. For example, a controlling shareholder does not necessarily have the right to buy and sell

⁵² Macey, *supra* note 21, at 34.

⁵³ *See id.* at 34 ("in no case has the Delaware Supreme Court held that directors will be permitted to *prefer* the interests of other constituencies over shareholders. Nor has the court decreed that they *ought*, as a normative matter, to take such interests into account.").

⁵⁴ *See* discussion *infra* Part III.B. Although certain states' "other constituency statutes" *permit* corporate officers to consider other constituencies' interests in decision-making, no state has *imposed* a fiduciary duty on officers to weigh non-shareholder interests. Thus, the reasons for nationwide refusal to impose such a duty must be understood.

⁵⁵ *See* Greenfield, *supra* note 15, at 288.

⁵⁶ *Id.*

⁵⁷ *Id.* at 289.

⁵⁸ *See id.* at 288 (stating that "[s]hareholders contribute the capital and hire the management. . . . The authority of the corporation ultimately rests with them.").

⁵⁹ *See* Singer, *supra* note 18, at 622 (explaining that "[p]roperty rights are more often shared than unitary, and rights to use and dispose of property are never absolute.").

⁶⁰ *Id.*

⁶¹ *See id.*

⁶² *See id.*

stock as she pleases, as it is unlawful for her to benefit from her dominant position in the company and deprive minority shareholders their rights.⁶³ A shareholder's ability to make unregulated stock purchases and sales is also restricted by Rule 10b-5 of The Securities and Exchange Act of 1934.⁶⁴ The Securities and Exchange Commission interpreted Rule 10b-5 to require "corporate insiders," such as controlling shareholders, who possess material, non-public information to either disclose that information to the public or abstain from trading.⁶⁵ Thus, the law does not isolate shareholder property rights from governmental intrusion when the public interest warrants regulation.⁶⁶ Consequently, shareholder property rights cannot alone justify limiting fiduciary protections to shareholders.⁶⁷

The property-based justification of shareholder dominance is also objectionable on the ground that it illogically confers ownership status solely to shareholders. Just like shareholders own shares, bondholders own bonds, suppliers own their inventory, and workers own their labor.⁶⁸ All these groups contribute what they own to the corporation, yet it is only the shareholders' contribution of money for shares that grants ownership status.⁶⁹ A law affording shareholders lone beneficiary status assumes that there is something distinctive about the act of contributing money that justifies extending fiduciary protections only to shareholders.⁷⁰ However, in light of a corporation's obvious need for employees' labor, including their development of firm-specific skills unlikely to be useful at other jobs, corporate law should safeguard their investment of labor.⁷¹ Recognition of a broader concept of ownership, which considers the diverse nature of stakeholder contributions, may warrant extending ownership status to all contributors to the corporation and consequently provide the protection of fiduciary duties to non-shareholder stakeholders as "owners" of the corporation.⁷²

Lastly, even assuming that consideration of a stakeholder's interest in corporate decision-making depends on that stakeholder's property rights, workers possess such property rights arising from their reliance interest in their jobs.⁷³ Although the Sixth Circuit has rejected the legal recognition of workers' property rights in the corporation

⁶³ See *Jones v. H. F. Ahmanson & Co.*, 460 P.2d 464 (Cal. 1969) (illustrating how the California Supreme Court held that a controlling group of shareholders, with 85 percent of the company's shares, violated their fiduciary duty to the minority shareholders by exchanging their expensive, unmarketable shares in the company with cheaper shares of another company they owned and selling these new, cheaper shares to the public at a great profit. The acts of the majority shareholders created a public market for their otherwise unmarketable shares, while the minority shareholders had no market to sell their shares. Therefore, the controlling group of shareholders breached their obligation to the minority shareholders.).

⁶⁴ See Securities and Exchange Commission Rule 10b-5, 17 C.F.R. §240.10b-5 (West 2007).

⁶⁵ See *In re Cady Roberts & Co.*, Exchange Act Release No. 34-6668, 40 S.E.C. 907 (1961).

⁶⁶ See *id.* at 913 (stating that "[w]e cannot accept respondents' contention that an insider's responsibility is limited to existing stockholders and that he has no special duties when sales of securities are made to non-stockholders.")

⁶⁷ See *id.*

⁶⁸ See Greenfield, *supra* note 15, at 293.

⁶⁹ *Id.*

⁷⁰ *Id.* at 293-294.

⁷¹ See Katherine Van Wezel Stone, *Employees As Stakeholders Under State Nonshareholder Constituency Statutes*, 21 STETSON L. REV. 45, 53 (1991).

⁷² See Greenfield *supra* note 15, at 293 (explaining that "the law has long recognized that 'ownership' assumes obligations as well as rights.>").

⁷³ See Singer *supra* note 18, at 621.

stemming from reliance on their jobs due to a lack of precedential authority,⁷⁴ Joseph Singer argues that common law doctrines and principles provide enough precedential support to acknowledge workers' property rights that arise from their relationship with companies.⁷⁵ For example, courts recognize easements, which grant one a property right, arising from reliance on access to another's land, to use that other person's land for a certain purpose.⁷⁶ Courts also recognize property rights arising from adverse possession, which is an involuntary transfer of land from the initial owner to another party because the latter has relied upon his use of the land like an owner for a statutorily prescribed number of years.⁷⁷ Recognizing the numerous legally enforceable property rights that have grown out of reliance on access to property or on the continuation of a relationship, Singer concludes that the Sixth Circuit, in *Youngstown*, could have drawn on such property rights as precedential authority to extend to workers a property right in the Corporation.⁷⁸

Therefore, the property-based justification of shareholder dominance not only ignores the divisible and limited nature of "ownership", but also does not justify shareholder dominance given that workers can also be considered "owners" of the corporation and can have reliance-based property rights.

C. The Agency-Based Justification for Shareholder Dominance

Advocates of shareholder dominance in corporate law also defend excluding non-shareholder interests in boardroom deliberations by postulating that corporate law should solely address the conflicts of interest that arise from a corporation's separation of ownership and control.⁷⁹ This theory of the corporation, initially proposed by Adolf Berle and Gardiner Means,⁸⁰ acknowledges that separation of ownership and control, with the former resting with shareholders and the latter with management, was increasingly characteristic of large corporations and examined the inevitable conflicts of interest between the two groups.⁸¹ Generally, whereas shareholders sought corporate decisions that maximize profits, managers would use their control to pursue their own

⁷⁴ See Local 1330, *United Steel Workers of America v. United States Steel Corp.*, 631 F.2d 1264, 1280 (6th Cir. 1980) [hereinafter *Youngstown*]. In *Youngstown*, the United States Steel Corporation made a decision to shut down its Youngstown plant although the entire town had come to rely on the United States Steel Corporation for its livelihood. *Id.* at 1265. The workers of the Corporation asserted that they had acquired a property right in the Corporation, in the nature of an easement, due to the long-established relationship between them and the Corporation. *Id.* at 1280. They further alleged that this property interest in the Corporation required the management to adopt strategies other than, or in addition to, shutting down. *Id.* The Sixth Circuit, however, rejected the workers' arguments, did not recognize a worker property right based on reliance, and refrained from imposing a duty on the Corporation to consider the impact of the plant closing on the workers because the court determined that it lacked precedential authority to create such a property right. *Id.* at 1281-82.

⁷⁵ Singer, *supra* note 18, at 621.

⁷⁶ *Id.* at 665-666.

⁷⁷ *Id.* at 668-669.

⁷⁸ *Id.* at 678.

⁷⁹ David Millon, *Theories of the Corporation*, 1990 DUKE L.J. 201, 220-21 (1990).

⁸⁰ See generally ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932) (analyzing trends in corporate development).

⁸¹ Millon, *supra* note 78, at 220-21.

interests such as entrenching themselves.⁸² To resolve the conflict, Berle and Means viewed management's role as trustee for the shareholders.⁸³ Accordingly, the legitimacy of management's exercise of control depends on whether management's decision fairly protects the interests of the shareholders.⁸⁴ Corporate activity is understood as shareholders, as individual property owners, simply pursuing their business interests through their fiduciary, management.⁸⁵

The proposition that derives from this understanding of corporate activity is that corporate law's aim should be to address and regulate the accountability problems that flow from the trustee relationship.⁸⁶ Due to the numerous potential conflicts between shareholders and managers,⁸⁷ contractarians view managers as "less than perfect agents" who impose agency costs on shareholders.⁸⁸ As such, they conclude that the purpose of fiduciary duties is to reduce these agency costs by creating a legal mechanism through which shareholders can ensure that management acts in their best interest.⁸⁹

Although corporate law must address the inevitable agency problems that flow from a separation of ownership and control, it does not follow that corporate law should ignore agency costs incurred by other corporate stakeholders, such as workers. In the labor context, workers also bear heavy agency costs.⁹⁰ To be sure, workers are not technically "masters" whose interests must be considered by the "servant" managers. Nonetheless, workers bear "agency costs" in the same way shareholders do – both groups contribute something of value to the corporation and must depend on management to act honestly and loyally in maximizing the return on their input and sharing that return with them.⁹¹ For example, management's neglect of worker interests may result in lower pay or less secure jobs for workers, thereby reducing the return on their labor contribution.⁹² Therefore, so long as reducing agency costs warrants granting the protections of fiduciary obligations to shareholders, similar agency cost reduction concerns justify granting workers fiduciary protections.

Furthermore, acknowledging that workers have many less market protections than shareholders to reduce their agency costs, it follows that they require the protection of fiduciary obligations even more than shareholders do.⁹³ Workers have less informational rights than shareholders⁹⁴ and, accordingly, possess less of an ability to analyze the

⁸² *Id.*

⁸³ *Id.* at 221.

⁸⁴ *Id.* at 224.

⁸⁵ *Id.* at 223-224.

⁸⁶ *Id.*

⁸⁷ Greenfield, *supra* note 15, at 296. For example, while shareholders would like managers to work as hard as possible to maximize profits, managers, whose salaries are often fixed, may not work as hard as the shareholders would like because they do not reap the gains or suffer the losses of their work. *Id.* Also, whereas managers would like to take low-risk decisions to minimize the risk of bankruptcy and retain their jobs, shareholders prefer the corporation to make high-risk decisions because the high risk could be eliminated through diversifying securities in one's portfolio. *Id.*

⁸⁸ *Id.*

⁸⁹ *Id.*

⁹⁰ *Id.* at 299-300.

⁹¹ Greenfield, *supra* note 15, at 300.

⁹² *Id.*

⁹³ *Id.* at 303.

⁹⁴ By granting only shareholders a general right to inspect corporate books, Delaware law is illustrative of the information rights held by shareholders and not workers. 8 DEL. CODE ANN. tit. 8, § 220(b) (West

impact of managerial decisions on their interests.⁹⁵ Also, unlike shareholders, workers do not vote for directors and major corporate actions,⁹⁶ removing any management fear of worker backlash for ignoring their interests. And even if they do have the information to determine that management is not acting in their interest, workers cannot respond as effectively as shareholders.⁹⁷ It is more difficult for a worker to quit than a shareholder to sell because a worker's input, labor, is less diversified, the labor market is less liquid, and labor is less mobile.⁹⁸ This difficulty is compounded when the worker has developed firm-specific skills, because the employer knows that it is that much harder for the worker to find a new job at a different company that pays a comparable wage.⁹⁹

2007) (stating that “[a]ny stockholder, in person or by attorney or other agent, shall, upon written demand under oath stating the purpose thereof, have the right during the usual hours for business to inspect for any proper purpose, and to make copies and extracts from: (1) The corporation's stock ledger, a list of its stockholders, and its other books and records; and (2) A subsidiary's books and records A proper purpose shall mean a purpose reasonably related to such person's interest as a stockholder.”); *Seinfeld v. Verizon Comm'n, Inc.*, 909 A.2d 117, 123-25 (Del. 2006) (noting that its determination that plaintiff did not show a “proper purpose” to inspect the corporation's books by failing to cite even “some evidence” to establish a “credible basis” of management wrongdoing is only the second time the Delaware Supreme Court has prohibited a plaintiff from inspecting the corporation's books due to his inability to meet even this “lowest possible burden of proof”).

⁹⁵ See Greenfield, *supra* note 15, at 303 (explaining that “[i]t is not clear . . . why corporate law should step in to reduce further the agency costs between managers and shareholders yet not between managers and workers.”).

⁹⁶ See 8 DEL. CODE ANN. tit. 8, § 211(b) (West 2007) (stating that “[u]nless directors are elected by written consent in lieu of an annual meeting as permitted by this subsection, an annual meeting of stockholders shall be held for the election of directors on a date and at a time designated by or in the manner provided in the bylaws.”); William A. Klein and John C. Coffee state:

By statute, common shareholders have the right to vote (at annual or specially called meetings) for the election of directors and on certain “fundamental matters.” Under most state statutes, the “fundamental matters” that require a common shareholder vote include: (1) mergers involving the corporation (except, under some statutes, when the corporation acquires a much smaller firm), (2) any amendment to the certificate of incorporation, (3) the sale of substantially all the corporation's assets, and (4) liquidation.

WILLIAM A. KLEIN & JOHN C. COFFEE JR., *BUSINESS ORGANIZATION AND FINANCE: LEGAL AND ECONOMIC PRINCIPLES* 204 (8th ed. 2002).

⁹⁷ Greenfield, *supra* note 15, at 302.

⁹⁸ *Id.* Whereas shareholders can avoid suffering the financial harm by investing in potentially hundreds of stocks and offsetting investment losses from a poorly managed company with gains from other investments, workers typically hold one or two jobs and face so they suffer more due to possible job and income loss caused by poor management. *Id.* Also, the labor market is less liquid than the stock market because selling and buying shares can easily and quickly be done in an efficient stock market without any tangential costs, unlike the potentially lengthy process of quitting a job and finding a comparable substitute and the costliness of relocating and foregoing income during unemployment. *Id.* Due to the labor market's lack of liquidity and workers' inability to diversify investment of labor, workers are more pressured than shareholders to continue investing in a firm that neglects their interests. *Id.* As such, workers cannot rely on the sort of market protections available to shareholders to reduce agency costs and accordingly require relatively more protection from fiduciary duties. *Id.*

⁹⁹ Jonathan Macey, *Externalities, Firm-Specific Capital Investments, and the Legal Treatment of Fundamental Corporate Changes*, 1989 DUKE L.J. 173, 191-92 (1989). When workers are required to develop firm-specific skills through training, they often bear large opportunity costs in foregoing employment as unskilled laborers because they are paid a lower wage than unskilled laborers during training in return for a promise of a substantially higher, specified wage after the training period. However, these skilled workers' foregone costs present firm managers the opportunity to take advantage of the workers' sunk opportunity costs after the training period by renegeing on their earlier promise of

Therefore, both because workers bear agency costs similar to those borne by shareholders and because workers possess fewer market protections to reduce their agency costs, workers also need the protection of fiduciary duties as an agency cost-reduction method.

D. The Shareholder as Residual Claimant Justification for Shareholder Dominance

In addition to supporting shareholder dominance based on property rights and agency cost-reduction theories, advocates of shareholder dominance contend that shareholders' status as residual claimants in the corporation alone justifies shareholder dominance.¹⁰⁰ Shareholders are residual claimants of the corporation because, when a firm liquidates, they will be paid last out of firm assets.¹⁰¹ Unlike other stakeholders whose claims on corporate assets are fixed and limited and who shy away from risky investments as they stand to suffer from any investment loss without a corresponding opportunity to directly share in firm profits,¹⁰² shareholders have an unlimited interest in pursuing firm profitability due to their ownership of all remaining firm assets after payment to other claimants.¹⁰³ As such, fiduciary duties run solely to shareholders because, as residual claimants, "[t]he gains and losses from abnormally good or bad performance are the lot of the shareholders, whose claims stand last in line."¹⁰⁴

Also owing to their residual interest in the firm, shareholder dominance supporters argue that shareholders' interests most closely reflect the interests of the firm.¹⁰⁵ Shareholder interests are most representative of the entire firm's interests because they have the greatest incentive to maximize long-term profits.¹⁰⁶ Thus, advocates of shareholder dominance reason that not only do shareholders equitably deserve the sole protection of fiduciary duties due to their greater risk-bearing investment, but that they

substantially higher post-training wages and offering wages only slightly above unskilled laborer wages. Managers remain confident that the skilled workers will accept even a slightly higher wage because the opportunity costs they already bore in foregoing work as unskilled laborers are sunk. Managers are thus especially capable of engaging in opportunistic behavior harmful to skilled laborers by benefiting from the low wages they paid these workers during training without compensating their sacrifice as promised. *Id.* O'Connor, *supra* note 46, at 923.

¹⁰⁰ Black, *supra* note 34, at 4.

¹⁰¹ Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 447 (2006).

¹⁰² *Id.* Workers' claim on corporate assets is their salary or wages, and is commonly fixed. Similarly, bondholders and creditors have limited interests in a corporation's profitability; mostly, they are concerned with the firm's ability to repay them with the set interest. *See id.* (stating that "[t]he interests of all other stakeholders are poor proxies for societal wealth because all other stakeholders have limited claims on the assets of the corporation. Because they will bear the downside of any risk without the ability to capture its upside potential, their incentive is to minimize risk to the corporation. The shareholder, however, is in a unique position.")

¹⁰³ *Id.*

¹⁰⁴ *See* Easterbrook & Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395, 403 (1983).

¹⁰⁵ Velasco, *supra* note 100, at 447. Whereas other stakeholders are concerned primarily with securing their fixed returns from the firm (either through compensation, loan repayment, or interest), shareholders have a strong incentive to maximize firm profits. Unlike other stakeholders who risk suffering from firm losses (through job insecurity or not receiving loan payments) but stand to gain little from gains, shareholders bear the whole weight of risk. Investment losses' reduction in firm capital results in lower share values for shareholders, while any gains are reflected in a boost in share value and a larger pool of assets for them to share after firm obligations to other claimants are met. Thus, shareholders alone carry the incentive to pursue firm profitability beyond the level required to simply meet firm obligations. *Id.*

¹⁰⁶ *Id.*

are also best-suited to hold fiduciary protections because they serve as the best representatives of the firm's interest in profit-maximization.¹⁰⁷

A theory granting shareholders fiduciary protections due to their residual interest suffers from a narrow conception of residual interest because it focuses only on the interests at stake in liquidation and not the spectrum of other, more likely, future possible outcomes.¹⁰⁸ When the various interests in other future outcomes are considered (such as interests in undergoing an investment, pursuing a merger or acquisition, laying off employees, closing a plant, issuing convertible bonds), the link between firm profitability and the expectations of all stakeholders becomes clear, whether those expectations are implicit or explicit.¹⁰⁹ Stakeholders' future expectations, or expected values, shape their incentives to act to increase firm value.¹¹⁰ As such, "residual interest" is more accurately defined as involving "any situation in which the expected value of a contracting party's future dealings with the firm increases as the firm's value increases, and decreases as the firm's value decreases."¹¹¹ Furthermore, this reformulation of "residual interest" requires adjusting the definition of "residual claimant" from a stakeholder with an interest in liquidation to "a person whose relationship to the firm gives rise to a significant residual interest in the firm's success."¹¹² The latter definition explains how an employee who has developed firm-specific skills has a residual interest in that firm concerning corporate decisions that may bankrupt the firm because his particular skills will likely be useless and uncompensated in another job.¹¹³ Similarly, a creditor has a residual interest in the corporation regarding issuances of dividends that may render the debtor-firm unable to fulfill debt obligations and frustrate his contractual expectation to be repaid.¹¹⁴ As such, residual interests in a firm may include not only what a stakeholder is paid in the unlikely event of liquidation, but also the diverse interests of a stakeholder for whom the expected value of future dealings with the firm is positively correlated to an increase or decrease in firm value.¹¹⁵

Under such a conception of "residual interest," a company's workers – along with its creditors, suppliers, and local community – also retain a residual interest in the corporation.¹¹⁶ For employees who depend on stock options or profit-sharing as compensation, an increase in firm value raises their compensation, thereby affording them a residual interest in the firm. Even for employees with fixed wages, an increase in

¹⁰⁷ *Id.*

¹⁰⁸ Black, *supra* note 34, at 18-19. Black cited the infrequency of firm liquidations relative to ongoing business transactions, the triviality of corporate decisions during liquidation, and the likelihood that no substantial firm assets will remain after non-shareholder claimants are paid and concluded that rights in corporate law should not be distributed based on interests in liquidation only.

¹⁰⁹ *Id.* at 15. Stakeholders' explicit expectations arise from contract or statute, such as a convertible bondholder's contractual expectation to share in firm profitability with common shareholders upon the firm achieving a predetermined level of profit. *Id.* Implicit expectations result from expectations and likelihoods that form "implicit contracts," such as an employee's expectation that he will receive a salary raise if the firm profits are strong. *Id.* at 5.

¹¹⁰ *Id.* at 4.

¹¹¹ *Id.* at 15.

¹¹² *Id.* at 4.

¹¹³ See Black, *supra* note 34, at 3.

¹¹⁴ See *id.*

¹¹⁵ *Id.* at 5.

¹¹⁶ *Id.*

firm value may strengthen their job security, create funds for annual bonuses, or enhance the value of pension and retirement benefits.¹¹⁷ Accordingly, even if shareholders' residual claimant status warranted extending the protections of fiduciary duties to them, it does not require extending such protections solely to them, to the exclusion of other stakeholders.¹¹⁸ Indeed, grounding fiduciary duties on protecting residual claimants yields the problematic outcome of offering all stakeholders these protections.

The residual interest-based justification for shareholder dominance is flawed also because its assertion that shareholders' interest is most representative of the firm's interest ignores the effects of portfolio diversification on shareholders' considerations.¹¹⁹ Due to the practically risk-immunizing effects of portfolio diversification, common shareholders tend to prefer managements to undertake risky projects¹²⁰ that, if successful, are estimated to generate large profits to less risky projects carrying a lower, but more secure, return.¹²¹ Yet the shareholders' investment choice may not coincide with all stakeholders.¹²² Consequently, a management that undertakes such a risky investment favored by shareholders may do so at the expense of other stakeholders.¹²³ Equally significant, these same stakeholders, who alone bear the costs of Project C's possible failure, are not owed any of the fiduciary duties owed to risk-diversifying shareholders.¹²⁴ Thus, a theory of shareholder dominance resting on a residual interest justification suffers not only from a narrow conception of residual interest, but also from mistakenly assuming that shareholder and firm interests coincide.

E. Shareholder Dominance Justified by Shareholders' Need for Contractual Gap-Filling

Some shareholder rights advocates, namely contractarians, support exclusively allocating fiduciary duties to shareholders by basing such an allocation on the nexus of contracts theory of the corporation.¹²⁵ According to contractarian theory, the various stakeholders in a corporation are suppliers of different inputs and the corporation is

¹¹⁷ Greenfield, *supra* note 15, at 306.

¹¹⁸ Jonathan R. Macey & Geoffrey P. Miller, *Corporate Stakeholders: A Contractual Perspective*, 43 U. TORONTO L.J. 401, 403 (1993) (examining the role of the law in privileging certain stakeholders' interests).

¹¹⁹ Macey, *supra* note 21, at 29.

¹²⁰ KLEIN & COFFEE, *supra* note 49, at 268 ("Most shareholders invest only a small proportion of their total wealth in the shares of a single corporation; they diversify their investment portfolios. Shareholders may be risk averse with respect to their entire portfolios of investments but not with respect to the individual components of those portfolios.") *Id.* An exception to shareholders' willingness to bear risk may be controlling shareholders (who likely are heavily invested in one company) and investors who choose to invest in a small number of firms. *See id.*

¹²¹ Macey, *supra* note 21, at 29. For example, as Jonathan Macey illustrates, with \$1 million to invest, between Project C, bearing a 50% chance of generating \$500,000 and 50% chance of generating \$10 million, and Project A, with a 50% chance of yielding \$1 million and 50% chance of yielding \$5 million, shareholders would rather a corporation invest in the riskier Project C due to its higher expected return. *Id.* For shareholders, Project C's risk of losing \$500,000 can be eliminated, or at least minimized, by investing in a large number of diverse corporations, many of whose risks are likely to result in large gains. *Id.*

¹²² *Id.* Assuming that this hypothetical corporation owes employees and creditors \$1 million, the shareholders' choice of Project C burdens the employees and creditors with a 50% likelihood that they will not be paid what they are owed. *Id.*

¹²³ *Id.* at 30.

¹²⁴ *Id.*

¹²⁵ Millon, *supra* note 78, at 231.

merely the sum of the agreements among those various stakeholders, or suppliers.¹²⁶ A corporation is nothing but the product of individual suppliers freely contracting according to the contributions they are willing to make and the benefits they aim to derive.¹²⁷ The outcome of this theory is a vision of corporate law that imposes only those rules that duplicate the terms individual stakeholders would agree upon through actual negotiations.¹²⁸ Thus, to the extent stakeholders wish to protect their interests through certain means, they are free to bargain for them. It is not the province of corporate law, however, to grant rights and impose obligations where none have been bargained for.¹²⁹ Thus, for contractarians, similar to any other right or obligation, fiduciary duties are rights that parties must negotiate for and the law should impose owing such duties to only those stakeholders who would contract for them.¹³⁰

Contractarians then advocate that, as the stakeholder group willing to pay the most for fiduciary duties, the law should impose owing such duties only to shareholders.¹³¹ Though contractarians acknowledge that other groups of stakeholders also value fiduciary duties, they surmise that other stakeholder groups do not value them as much as shareholders.¹³² Contractarians reason that shareholders value being owed fiduciary duties the most because they face severe and unique contracting problems with management.¹³³ While all other stakeholders are able to address their concerns through contract, it is not feasible to predict and specify in advance how management should react to a wide range of unforeseeable contingencies.¹³⁴ For example, as workers are primarily concerned with wages, hours, and working conditions, their concerns are easily predictable and suitable to contract. Indeed, pension guarantees, work hours, cost-of-living wage adjustments are among the many provisions workers can bargain for.¹³⁵ Conversely, a contract cannot so easily predict and address all situations in which shareholders' interest in maximizing firm profits directs management to act a certain way.¹³⁶ Such contingencies can only be addressed by an open-ended promise by management to act with care, loyalty, and honesty.¹³⁷ As such, fiduciary obligations are owed to shareholders merely as a device to fill the unspecified terms of contingent contracts between management and shareholders.¹³⁸

Moreover, according to contractarians, an understanding of fiduciary duties as a mechanism to address contracting hurdles not only justifies allocating fiduciary protections to shareholders, but also supports exclusively allocating these protections to shareholders.¹³⁹ This leap from granting shareholders such protections to limiting the scope of fiduciary protections to them is made due to the greater value shareholders place

¹²⁶ *Id.*

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ *Id.*

¹³⁰ *See id.*

¹³¹ Macey & Miller, *supra* note 118, at 416.

¹³² *Id.*

¹³³ *Id.*

¹³⁴ *Id.* at 407.

¹³⁵ *Id.* at 417.

¹³⁶ Macey & Miller, *supra* note 118, at 417.

¹³⁷ *Id.*

¹³⁸ *Id.* at 407.

¹³⁹ *Id.* at 410.

on fiduciary duties relative to other stakeholders and the diminished value of fiduciary duties when shared among groups of stakeholders.¹⁴⁰ Consequently, the law should recognize this result as what the parties would have agreed upon and thereby grant shareholders the sole protection of fiduciary duties as a method of addressing shareholder-specific contracting problems.

The contractarian rationale for shareholder dominance is flawed because it neglects both the lack of workers' bargaining leverage and the contingencies workers also face in bargaining.¹⁴¹ Relying on the contracting process to yield employment contracts that adequately and fairly address worker interests wrongly assumes that workers and management possess equal leverage in negotiations.¹⁴² For instance, Joseph Singer cites how in 1992, "given the legality of hiring replacement workers during a strike, the low percentage of US workers who are union members, the availability of a reserve army of the unemployed, the relatively low wages in the service sector, the increasing mobility of capital, and increasing international competition," the Caterpillar company forced one of the strongest US unions to end its strike simply by threatening to replace all the workers.¹⁴³ The reasons Singer cites for workers' unequal bargaining power are not confined to the strike he discusses; market forces unfavorable to workers regularly limit their bargaining ability.¹⁴⁴ Even the collective bargaining strength of some workers who are represented by unions possessing greater bargaining leverage than individual workers is tempered by the minimal worker-relevant issues subject to mandatory bargaining between employers and unions, unions' inability to prevent certain major corporate decisions harmful to workers, and the relatively low percentage of workers who are represented by unions.¹⁴⁵ Further, this disparity in bargaining power between contracting parties is likely to result in a contract that imposes exploitative terms on the weaker party, rather than a contract that reflects a "voluntary arrangement that maximizes the joint interests of both parties."¹⁴⁶ Thus, because of the exploitative employment contract terms that may result from depending on the contractual process, corporate law should not be unresponsive to worker interests.

Contractarians also wrongly limit fiduciary protections to shareholders due to their erroneous judgment that only shareholders face unforeseeable contingencies during the contracting phase, thereby neglecting the unpredictable events in workers' contracting process.¹⁴⁷ Restraints on the numerous forms of employer opportunism, inability to

¹⁴⁰ *Id.* at 410-11. For example, although shareholders may value fiduciary duties at \$75 and workers may value fiduciary duties at \$50, if fiduciary duties are shared by the two groups, each values them only at \$20 because corporate fiduciary duties become less valuable as they are dispersed onto additional groups. *Id.* Accordingly, the likely outcome through rational bargaining is granting shareholders fiduciary duties for \$75 less what the shareholders pay the workers for exclusive receipt of fiduciary duties, some amount greater than \$20. *Id.*

¹⁴¹ Greenfield, *supra* note 15, at 314.

¹⁴² *Id.*

¹⁴³ Singer, *supra* note 11, at 476.

¹⁴⁴ Greenfield, *supra* note 15, at 316.

¹⁴⁵ Richard Marens, *Getting Real: Stakeholder Theory, Managerial Practice, and the General Irrelevance of Fiduciary Duties Owed to Shareholders*, BUS. ETHICS Q., 273-293 (1999) (arguing that Stakeholder theorists have generally misunderstood the nature and ramifications of the fiduciary responsibilities that corporate directors owe their stockholders).

¹⁴⁶ Singer, *supra* note 11, at 491.

¹⁴⁷ Greenfield, *supra* note 15, at 315.

foresee future productivity goals, difficulties in outlining job security provisions, and the impossibility of describing the level of effort required by employees or the many facets that comprise general working conditions represent some of the worker-related issues that cannot easily or cost-efficiently be addressed at the employment contracting phase.¹⁴⁸ As a result, it is clear that unforeseeable contingencies also limit workers' ability to address all worker interests through contract.¹⁴⁹ Therefore, so long as contractual gap-filling for unforeseeable contingencies merits affording shareholders the protection of fiduciary duties, similar gap-filling motives justify extending these protections to workers.¹⁵⁰

Furthermore, relying on contract law to redress workers who are harmed due to a firm's action precludes workers from obtaining relief where the firm's harmful action was contrary to an implicit firm agreement, rather than an express contractual provision.¹⁵¹ For instance, when applying to the Township of Ypsilanti for a tax abatement on investments in two local plants, a General Motors spokesperson stated: "Upon completion of this project and favorable market demand, it will allow Willow Run to continue production and maintain profitable employment for our employees."¹⁵² Despite continued market demand, General Motors closed the Willow Run plant.¹⁵³ Nonetheless, General Motors was not found liable for the harm it inflicted on its Willow Run plant employees because the General Motors spokesperson's statement was not a "clear and definite contractual promise."¹⁵⁴ As the latter case demonstrates, contract law fails to guard worker interests also due to its failure to protect the non-contractual expectations of workers that arise from implied agreements.

II. FEASIBILITY OF GRANTING FIDUCIARY DUTIES TO WORKERS

Even if workers should be owed fiduciary duties due to their important status in the corporation and the ineffectiveness of current avenues to address their interests, in order to actually attain the protection of such duties, they must also be practically feasible.¹⁵⁵ Bernard Black keenly recognized the possibility that "no law yet devised can protect employees against perhaps the largest risk they face – not being hired in the first place."¹⁵⁶ If reforms in corporate law, such as the extension of fiduciary protections to workers, do more harm than good, then even the theoretical soundness of - and practical need for - additional worker protections do not validate extending fiduciary protections to

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ O'Connor, *supra* note 44, at 106.

¹⁵² Ypsilanti v. Gen. Motors Corp., 506 N.W.2d 556 (Mich. Ct. App. 1993).

¹⁵³ *Id.*

¹⁵⁴ *Id.* Compare Ypsilanti v. Gen. Motors Corp., 506 N.W.2d 556 (Mich. Ct. App. 1993) (holding that the company was not liable for the harm its employees suffered due to a plant closing after a company spokesperson assured employees that the plant would continue production) with Basic Inc. v. Levinson, 485 U.S. 224 (1988) (holding that the company was liable to shareholders for a company press release it issued falsely denying that it was involved in merger negotiations because this misrepresentation was "material" due to the substantial likelihood that a reasonable investor would consider it important in making an investment decision).

¹⁵⁵ Black, *supra* note 34, at 22.

¹⁵⁶ *Id.*

workers.¹⁵⁷ Thus, a proposal offering workers fiduciary protections must rely not only on the demonstrable need for additional safeguards for worker interests and the theoretical flaws in limiting fiduciary protections to shareholders.¹⁵⁸ Such a proposal must also account for the likely effects of its implementation and account for its drawbacks and obstacles.¹⁵⁹

A. The Problem Heterogeneous Worker Interests Poses for an Extension of Fiduciary Duties to Workers

A potential drawback of granting workers fiduciary protections is the impracticality of granting an entire worker population of a firm, with heterogeneous interests, a fiduciary duty to consider their interests.¹⁶⁰ Different groups of workers within a firm will have diverging interests and preferences regarding a certain corporate decision or transaction stemming from their different roles, employment contracts, ages, genders, experiences, seniority level, and mobility.¹⁶¹ For example, in designing a pension plan, younger workers will have much different interests than older workers.¹⁶² Similarly, in carrying out a plan to layoff workers, the interests of workers with seniority differ from new workers.¹⁶³ Thus, even if workers were owed fiduciary duties, the conflicting corporate decisions required by divergent worker interests would make it impossible to delineate exactly what actions managements must take in carrying out their obligations to workers.

The problem the heterogeneity of interests poses in extending fiduciary protections to workers is overstated, however, in light of the similar divergence of interests existing between groups of shareholders.¹⁶⁴ Although shareholders share the basic goal of maximizing the value of the company and their future distributions, there are numerous issues on which the views of different groups of shareholders will diverge.¹⁶⁵ Even on the issue of dividend distributions, shareholders may prefer different policies depending on how they will be taxed for those dividends.¹⁶⁶ More troubling conflicts may arise between shareholders who also have a contractual relationship with the firm and shareholders who are interested solely as investors.¹⁶⁷ Shareholders who are also officers, for example, are less inclined to favor risky decisions than shareholders who are merely investors in the firm.¹⁶⁸ Yet despite these divergent shareholder interests,

¹⁵⁷ See *id.*

¹⁵⁸ See *id.*

¹⁵⁹ See *id.*

¹⁶⁰ See Black, *supra* note 34, at 8.

¹⁶¹ See Henry Hansman, *Worker Participation and Corporate Governance*, 43 U. TORONTO L.J. 589, 593 (1993) (discussing direct worker participation in corporate governance).

¹⁶² *Id.*

¹⁶³ *Id.*

¹⁶⁴ *Id.* at 592.

¹⁶⁵ *Id.*

¹⁶⁶ See *id.*

¹⁶⁷ See *id.*

¹⁶⁸ See *id.*

the current regime of affording shareholders fiduciary protections has been workable.¹⁶⁹ The success of this current regime, in spite of the heterogeneity of shareholder interests, casts doubt on the alleged debilitating effect diverging worker interests will have in a corporate environment where workers are owed fiduciary duties. Since shareholders and workers have similarly divergent interests, and fiduciary shareholder protections prove workable despite shareholders varied interests, the extension of such protections to workers with varied interests should likewise prove workable.¹⁷⁰

Yet, one has to assume that the heterogeneous interests of both shareholders and workers place the same kinds of burdens on managements' fiduciary obligations. Indeed, if the reason heterogeneous shareholder interests have not prevented the effective application of fiduciary protections to shareholders does not apply to managements' affording fiduciary protections to divergent worker groups, the success of the current fiduciary regime does not justify extending fiduciary protections to workers with different interests.¹⁷¹ Therefore, before concluding that heterogeneity of worker interests does not render the extension of fiduciary protections to workers unworkable, the similarity between the effects of divergent shareholder interests and divergent worker interests on managements' fiduciary obligations must be established.¹⁷²

Because shareholders' largely mutual interests have ensured the workability of the current regime, it is likely that the mutual interests among workers will render extending fiduciary protections to them workable.¹⁷³ Due to shareholders' common goal of maximizing firm value and the value of distributions, situations in which shareholders' interests diverge have proven to be the exception.¹⁷⁴ Generally, tax issues and transactional relationships with the firm do not create friction in defining shareholder interests.¹⁷⁵ Likewise, the common characteristics of workers' interests, such as ensuring job security, humane working conditions, and fair wages, forecast a frequent convergence of worker interests to be considered by managements.¹⁷⁶ For instance, in *Youngstown*, it was not the workers' diverging interests that precluded carrying out a fiduciary duty to consider their interests.¹⁷⁷ In fact, the *Youngstown* plants' 3,500 workers and family members were unified in opposing management's neglect of worker interests in closing the plants.¹⁷⁸ Furthermore, the convergence of the *Youngstown* workers' interests in a plant closing is representative of a general unity of worker interests in many other corporate decision settings. For example, workers generally prefer decisions that value stability over expected return, and oppose risking bankruptcy by incurring huge liabilities

¹⁶⁹ See *id.* (noting that conflicts do not involve a problem of collective choice, but rather involves two-party bargaining. Additionally, clear and objective criteria are often applied to restrict range of acceptable outcomes).

¹⁷⁰ See *id.*

¹⁷¹ See *id.*

¹⁷² See *id.* at 592-93.

¹⁷³ See *id.* at 591-92.

¹⁷⁴ See *id.*

¹⁷⁵ See *id.* at 592.

¹⁷⁶ Greenfield, *supra* note 15, at 300.

¹⁷⁷ See *Youngstown*, 631 F.2d at 1282.

¹⁷⁸ See *id.* at 1265.

to finance takeovers.¹⁷⁹ The frequent convergence of shareholder interests counters the potentially disabling effect of owing differing shareholders fiduciary duties. Additionally, the common union of worker interests concerning corporate decisions, in which fiduciary duties are most relevant, averts the overstated debilitating impact of extending fiduciary duties to workers.

B. The Problem Managers Serving "Too Many Masters" Poses for an Extension of Fiduciary Duties to Workers

Even if the heterogeneity of worker interests does not render the extension of fiduciary protections to workers unworkable or impractical, such an extension may be unworkable because managements have the impossible task of having with to serve "too many masters."¹⁸⁰ The "too many masters" argument bases its skepticism regarding workers fiduciary protections on the premise that management cannot effectively owe fiduciary duties to different constituencies with different interests.¹⁸¹ In advancing this argument, the Committee on Corporate Laws of the American Bar Association's Section on Business Law asserted:

If directors are required to consider other interests as well, the decision-making process will become a balancing act or search for compromise. When directors must not only decide what their duty of loyalty mandates, but also to whom their duty of loyalty run (and in what proportions) poorer decisions can be expected.¹⁸²

Thus, recognizing management's duty to consider the interests of two, often conflicting, constituencies in corporate decision-making, the "too many masters" argument holds that extending fiduciary protections to workers encumbers managements with an impossible and irreconcilable obligation.

Resembling the overstatement of the heterogeneous worker interests problem, the "too many masters" argument also overstates the problematic effect of owing both shareholders and workers fiduciary duties for two reasons.¹⁸³ First, a recognition that corporations have traditionally owed fiduciary duties to multiple, often conflicting, classes of stockowners defeats the presumption that fiduciary duties cannot be owed to constituencies with conflicting interests.¹⁸⁴ For instance, despite preferred shareholders often preferring projects less risky than those favored by common shareholders, corporate boards and managers have typically been able to balance the interests of the two groups

¹⁷⁹ Christopher J. Smart, *Takeover Dangers and Non-Shareholders: Who Should Be Our Brother's Keeper?*, 1988 COLUM. BUS. L. REV. 301, 305-6 (1988) (discussing the lack of protection for non-shareholders in the event of takeovers).

¹⁸⁰ Macey & Miller, *supra* note 118, at 411 (arguing that stakeholder statutes confuse the legal landscape by forcing directors to please many masters with competing and conflicting interests).

¹⁸¹ *Id.*

¹⁸² The Committee on Corporate Laws, *Other Constituencies Statutes: Potential for Confusion*, 45 BUS. LAWYER 2253, 2269 (1990).

¹⁸³ Macey, *supra* note 21, at 33.

¹⁸⁴ *Id.*

in discharging their fiduciary duties.¹⁸⁵ The ability to serve both preferred and common shareholder interests establishes, at the very least, the possibility that boards and managers can practically owe fiduciary duties to two constituencies with conflicting interests.¹⁸⁶ Thus the conflicting interests of shareholders and workers do not in itself render the discharge of fiduciary obligations to both shareholders and workers an impossible and irreconcilable task.

Second, and more important, the friction between shareholder and worker interests does not make the requirement that managements serve more than one master impracticable because these two groups often share interests and objectives.¹⁸⁷ For example, procedures and policies that improve worker morale, because they assure workers' commitment to company goals by symbolizing appreciation of workers' contributions, are not only good for workers, but also shareholders.¹⁸⁸ In fact, a study examining shareholder support for proposals, sponsored by labor unions, found that labor-sponsored proposals received a significantly higher percentage of votes than proposals sponsored by private institutions and individuals and an equal percentage of votes as proposals sponsored by public institutions.¹⁸⁹ Moreover, labor proposals aimed at furthering worker interests, specifically, rather than seeking to improve corporate governance structures, generated only a slightly lower percentage of favorable votes in relation to other similar proposals.¹⁹⁰ Consequently, the studies indicate that shareholders and workers usually agree on corporate decisions, even when labor and management conflict. This support, that's statistically demonstrable, which shareholders lend to workers' interests helps resolve the potentially irreconcilable task of serving too many masters and further affirms that fiduciary protections can be extended to workers.¹⁹¹ Indeed, even if at times worker and shareholder interests conflict regarding important corporate decisions, the frequent convergence of their interests, at the least, justifies reducing the high degree of concern commonly arising from such conflicts.

C. Analysis of the Protection Afforded to Workers Under the German and Japanese Systems of Corporate Governance

In addition to the feasibility of extending fiduciary protections to workers as evidenced by managements' ability to consider heterogeneous worker interests and divergent interests between classes of stock, the success other countries have had in offering workers significant protections further settles the feasibility of such a proposal.¹⁹² Under both the German and Japanese systems of corporate governance, for

¹⁸⁵ *Id.*

¹⁸⁶ *See id.*

¹⁸⁷ *Id.* at 34-5.

¹⁸⁸ *Id.* at 35.

¹⁸⁹ Stewart J. Schwab & Randall S. Thomas, *Realigning Corporate Governance: Shareholder Activism by Labor Unions*, 96 MICH. L. REV. 1018, 1052 (1998).

¹⁹⁰ *Id.*

¹⁹¹ *See id.*

¹⁹² Gulati, *supra* note 35, at 172.

example, workers are afforded greater protections than they are under the US system.¹⁹³ In Germany, corporate management is split into a two-tier system, consisting of a supervisory Aufsichtsrat board and a managerial Vorstand board.¹⁹⁴ The Aufsichtsrat board, whose duties generally resemble duties of a US corporation's board of directors, is comprised in significant part by employee representatives in addition to shareholder representatives.¹⁹⁵ This board meets at regular intervals, receives audit and other information, sets goals for the corporation, and assess the performance of, and hires and fires the members of, the management board.¹⁹⁶ Thus, because the board that is responsible for the substantial tasks of delineating the corporation's objectives and evaluating managers' performance is composed in large part by employee representatives, the German system of corporate governance ensures consideration of worker interests in corporate decision-making.

Although the Japanese corporate governance regime differs from that of Germany in that it does not formally ensure concern for worker interests and shares the U.S. system's strong concern for shareholder primacy, corporate practices stemming from custom nevertheless assure Japanese workers that their interests will be taken into account.¹⁹⁷ One such Japanese custom is the practice of appointing long-term employees as directors of the corporation.¹⁹⁸ Although informal, this custom has assured that a worker perspective will permeate corporate policy.¹⁹⁹ Japanese corporate governance is also influenced by the banks that typically own between twenty and twenty-five percent of a company's stock.²⁰⁰ These banks play an important role in assuring the continuance of weak firms by waiving a portion of the debt in exchange for the borrower adopting a restructuring plan and the government promising to prevent bank failure.²⁰¹ In helping avert bankruptcy, the effect of these banks is to benefit stakeholders' interests such as workers' jobs, suppliers' contracts, and lenders' repayment.²⁰² Moreover, the stabilizing effect of these banks is complemented by the practice of cross-shareholding, under which two companies, such as a supplier and a customer, agree to own one percent or so of each other's common stock.²⁰³ In fact, more than fifty percent of large Japanese corporations is estimated to be held by both banks and cross-shareholders.²⁰⁴ By owning such large stakes in corporations, these bank and cross-shareholding arrangements stabilize companies' volatility to market pressure and thereby bar outside shareholder influence.²⁰⁵ Lastly, the traditional lack of shareholder suits against management, due to the judicial deference afforded business executives, further insulates Japanese companies from

¹⁹³ Mark J. Loewenstein, *Stakeholder Protection in Germany and Japan*, 76 TUL. L. REV. 1673, 1674 (2002) (examining the corporate governance mechanisms of Germany and Japan and their accommodation of stakeholders concerns).

¹⁹⁴ *Id.* at 1676-77.

¹⁹⁵ *Id.* at 1677.

¹⁹⁶ *See id.*

¹⁹⁷ *Id.* at 1685-6.

¹⁹⁸ *Id.* at 1686.

¹⁹⁹ *Id.*

²⁰⁰ *Id.* at 1687.

²⁰¹ *Id.*

²⁰² *Id.* at 1687-88.

²⁰³ *Id.* at 1688.

²⁰⁴ *Id.*

²⁰⁵ *Id.* at 1687-88.

market pressure and shareholder influence.²⁰⁶ The consequence of a system of corporate governance that effectively immunizes companies from shareholder influence and fills directorial vacancies with long-term employees is a structure protective of worker interests.²⁰⁷

The practical feasibility of extending directorial fiduciary protections to workers is thus reinforced by both the German and Japanese systems' ability to afford worker interests significant consideration via measures that guarantee representation of worker interests in corporate decision-making.²⁰⁸ The success of these two systems casts doubt on the allegedly hindering effects of managements owing fiduciary duties to both shareholders and workers. Admittedly, these systems' ability to respond to worker interests is not without sacrifice.²⁰⁹ For example, individual stock ownership in Germany is very low, with large banks and other institutions accounting for most stock ownership.²¹⁰ The dearth of individual stock ownership can arguably be linked in part to the minimal shareholder concern attendant to a system that grants labor a prominent role.²¹¹ Also, the presence of employees in German boardrooms makes decision-making more costly due to increased friction during boardroom deliberations and thereby reduces the board's ability to effectively monitor management.²¹² Likewise, the implicit guarantee of permanent employment in Japan pressures troubled companies to harm long-term competitiveness by sacrificing profits or value rather than employees.²¹³

Nonetheless, the trade-offs between values in a system that affords workers significant protections do not render the system infeasible or unworkable.²¹⁴ Such a system may value the US corporate governance system's goal of efficiency less, but efficiency is not the only goal worth pursuing.²¹⁵ Certainly, a system granting workers significant protections is not unfeasible simply because it gives primacy to goals such as worker interests, social peace between labor and capital, and economic democracy.²¹⁶ Thus, the sacrifices attendant the German and Japanese systems of corporate governance do not so much cast doubt on the feasibility of extending fiduciary protections to employees as it simply reflects a different weight assigned to goals such as efficiency and individual shareholder participation.²¹⁷ The success of the German and Japanese models of corporate governance reveals that, apart from the merits of the systems, at the very least, a system of corporate governance that ensures inclusion of worker interests in corporate decision-making is feasible and workable.

III. ALTERNATIVE FORMULATIONS AND EFFECTS OF FIDUCIARY DUTIES THAT AFFORD CONSIDERATION OF WORKER INTERESTS IN U.S. CORPORATE GOVERNANCE

²⁰⁶ *Id.* at 1688-89.

²⁰⁷ *Id.* at 1690.

²⁰⁸ *Id.*

²⁰⁹ *Id.* at 1674.

²¹⁰ *Id.* at 1675.

²¹¹ See Brett H. McDonnell, *The Curious Incident of the Workers in the Boardroom*, 29 HOFSTRA L. REV. 503, 515-16 (2000) (examining the role of employees in corporate governance).

²¹² See *id.* at 515.

²¹³ Loewenstein, *supra* note 192, at 1686.

²¹⁴ See McDonnell, *supra* note 209, at 525-26.

²¹⁵ *Id.* at 526.

²¹⁶ See *id.*

²¹⁷ See *id.*

Despite the demonstrated ability of a corporate governance system affording workers fiduciary protections to withstand potential drawbacks and although Germany and Japan offer models of systems that successfully grant workers broad protections, the advisability of a particular corporate governance system that extends fiduciary protections to workers ultimately depends on its likely effects.²¹⁸ If a system that extends fiduciary protections to workers is less efficient in addressing worker interests or burdens society with greater costs than other systems, it is not prudent to adopt it.²¹⁹ Thus, before recommending an extension of fiduciary protections to workers, alternative versions of such a system must be critically analyzed and their costs and benefits must be carefully weighed.

A. Analysis of an Absolute Extension of Fiduciary Duties to Workers

One version of providing workers fiduciary protections envisions the absolute extension of directors' fiduciary obligations to workers.²²⁰ Under this structure, a director's or manager's duties of care and loyalty require consideration of worker interests in making corporate decisions and engaging in transactions.²²¹ The fiduciary obligations owed to workers give them a right to sue directors and managers if corporate action is taken without due regard to their interests, in violation of the board's and management's duties of care and loyalty.²²²

Opponents of an absolute extension of fiduciary protections to workers question the desirability of an obligation to consider workers' interests in corporate decision-making partly because it broadens the protection managerial decisions are afforded under the business judgment rule.²²³ They contend that, in combination, workers' and shareholders' fiduciary duties expand managerial discretion so as to allow for almost any corporate action to be justified as in the interest of one group or the other.²²⁴ Thus, although designed to address the neglect that workers' interests have historically met in the boardroom, supporters of shareholder supremacy view corporate governance systems that extend fiduciary protections to workers as counterproductive because of their potential use as a shield for managerial initiatives that may be to the detriment of both shareholders and workers.²²⁵

Moreover, even if management plans to act in accordance with its dual fiduciary obligations, shareholder supremacy supporters argue that management's ability to carry out this duty is questionable due to the occasional, but significant, clash between worker and shareholder interests regarding a given decision.²²⁶ Although the empirical

²¹⁸ See Black, *supra* note 34, at 18.

²¹⁹ GREENFIELD, *supra* note 28, at 183.

²²⁰ See Singer, *supra* note 11, at 501.

²²¹ See *id.* (discussing possible interpretations of stakeholder laws).

²²² See *id.* (outlining argument in favor of interpretation of stakeholder laws to create a private right of action enforceable by workers).

²²³ *Id.* at 500.

²²⁴ *Id.*

²²⁵ *Id.*

²²⁶ See *id.* at 503-04 (stating that "[i]t will almost always be possible for management to argue that the policy it has adopted was intended to maximize shareholder gain at minimum to workers").

observation that worker and shareholder interests align more often than is commonly suspected suggests the practicality of extending fiduciary obligations to both groups,²²⁷ this suggestion must be tempered by the critical observation that the infrequent divergence of worker and shareholder interests often occurs concerning vital corporate acts. In fact, in a host of important corporate decisions, shareholder and worker interests are squarely at odds with one another.²²⁸ Indeed, workers are commonly heavily invested in divisive corporate decision-making situations, where management must act in the interests of shareholders due to their exclusive role as fiduciary beneficiaries.²²⁹ The decision to close a company plant illustrates the dichotomy of shareholder and worker interests because, although a plant closing is likely to be opposed by workers concerned with job loss, the positive effect that it may have on the company's net profit may prompt shareholders to support it.²³⁰ Shareholders are often willing to bear the risk of bankruptcy inherent in some risky corporate transactions due to the risk-minimizing effect of portfolio diversification, even though bankruptcy will strip workers of their jobs.²³¹ If plant closings or layoffs will produce higher profitability, shareholders may support them, even at the expense of employees.²³² The infrequency of such conflicts, as

²²⁷ See discussion *supra* Part II.B (refuting the "too many masters" argument; recognizing frequent convergence of worker and shareholder interests).

²²⁸ See Jeffrey G. MacIntosh, *Designing an Efficient Fiduciary Law*, 43 U. TORONTO L.J. 425, 443 (1993) (stating that "[w]here multiple constituencies have standing. . . there is no guarantee that all will share the same view of the social welfare function."

²²⁹ See Terry O'Neill, *Employees' Duty of Loyalty and the Corporate Constituency Debate*, 25 CONN. L. REV. 681, 687 (1993) (discussing mechanisms to accomplish redistribution of wealth from employees to shareholders).

²³⁰ Illustrating the sort of vital corporate decisions on which shareholders and workers disagree, The Committee on Corporate Laws wrote:

[A]dding other constituencies provisions to state corporation laws may have ramifications that go far beyond a simple enumeration of the other interests directors may recognize in discharging their duties. Directors might have a duty to oppose a transaction with whatever means are available because it would have a demonstrably adverse impact upon one or more of the constituencies (e.g., the acquirer plans to move the headquarters from the small town in which the company had been rooted for decades resulting in community disruption and loss of jobs). Or directors might be called upon to decide how much of the premium over market price being paid in an acceptable transaction should be allocated among the various constituencies (e.g., how much should accrue to communities in which plants might be closed; how much should be allocated to the terminated hourly employees; and how much should be allocated to a supplier who might lose his market).

The Committee on Corporate Laws, *supra* note 182, at 2269-70.

²³¹ Greenfield discusses shareholders' immunity from risky corporate decisions that result in investment losses:

If we are to believe the assumptions of the contractarians, shareholders invest in a number of different companies and thus have diversified their portfolios. They are therefore risk neutral (and perhaps even risk prone) with respect to the decisions of any specific company. Diversified shareholders prefer that the management of any particular company they invest in makes decisions that maximize the expected value of the results, even if the results also are highly variable. That is, shareholders will tend to prefer risky decisions that may provide high payoffs but risk bankruptcy over decisions that provide lower returns but have less risk of pushing the firm into liquidation.

Greenfield, *supra* note 15, at 308.

²³² *Id.*

indicated by the empirically demonstrable common convergence of worker and shareholder interests, does not lessen their magnitude when they do arise.²³³ Consequently, shareholder supremacy advocates conclude that an absolute extension of fiduciary protections to workers will often be impractical and unworkable.²³⁴

B. Analysis of Fiduciary Duties Owed to Workers Under "Other Constituency Statutes"

"Other constituency statutes"²³⁵ can also be interpreted to give rise to a corporate governance system that extends more limited fiduciary protections to workers.²³⁶ Under this interpretation, other constituency statutes permit, but do not compel, management to consider the interests of non-shareholder constituencies, such as workers, in making certain specified corporate decisions.²³⁷ Notably, however, these other constituency statutes do not give the non-shareholder constituencies a private right of action with which to seek recourse when their interests are not considered.²³⁸ Thus, the statutes permit worker interests to be considered in boardroom deliberations, but do not impose a legally enforceable obligation on management to do so.²³⁹

Despite the permissive nature of other constituency statutes, shareholder supremacy advocates nevertheless oppose them.²⁴⁰ The permissive nature of such statutes effectively responds to the "too many masters" argument²⁴¹; however, these permissive statutes provide managerial decision-makers the same shield they are afforded under the system of absolute fiduciary obligation to both shareholders and workers.²⁴² Just as owing fiduciary duties to both groups in every corporate scenario allows management to justify every action as benefiting one of the groups, the discretion

²³³ See *supra* notes 228-230 and accompanying text.

²³⁴ Macey, *supra* note 21, at 43-4. But see discussion *infra* Part III.C.

²³⁵ See Committee on Corporate Laws, *supra* note 182, at 2253 (defining "other constituency states").

²³⁶ See Singer, *supra* note 11, at 499-500 (noting scholarship that argues in favor of interpreting stakeholder to contain a private right of action).

²³⁷ See e.g., N.Y. BUS. CORP. L. § 717(b) (2007) (stating corporate directors "entitled to consider" effects on employees and customers).

²³⁸ Singer, *supra* note 11, at 499-500.

²³⁹ See *id.*

²⁴⁰ See Millon, *supra* note 79, at 234-36 (noting recent state law modifications to incorporate concerns about non-shareholder constituencies and responses to them).

²⁴¹ Arguing that "other constituency statutes" do not excessively burden managers in allowing them to consider the interests of many constituencies with potentially conflicting interests but, rather, benefit managers due to their permissive nature and unenforceability, Macey states:

In one view, the "too many masters argument" implies that nonshareholder constituency statutes make life more difficult for corporate managers and boards of directors. The better view is that such statutes simplify life for incumbent managers of the large, public corporation. After all, virtually any management decision, no matter how arbitrary, can be rationalized on the grounds that it benefits some constituency of the corporation Thus, the primary beneficiaries of nonshareholder constituency statutes are incumbent managers, who can justify virtually any decision they make on the grounds that it benefits some constituency of the firm. The benefits to the constituencies are, at best, weak. Strong support for this assertion lies in the fact that not only are these statutes (with a single exception) permissive, but they also do not afford standing to sue to any of the nonshareholder constituencies that they purportedly are designed to benefit.

See Macey, *supra* note 21, at 31-2.

²⁴² *Id.*

managers have under the permissive statute to consider workers' interests also clearly permits justifying poor or self-interested management decisions simply by asserting that a decision benefits workers.²⁴³ Therefore, as viewed by shareholder supremacy advocates, other constituency statutes' aim to encourage consideration of worker interests will be defeated by their use as a management defense mechanism.²⁴⁴

Interestingly, workers' rights advocates often join their opponents in contesting the prudence of other constituency statutes.²⁴⁵ For instance, Joseph Singer, an advocate of worker-related changes in corporate law, acknowledges that these statutes may function solely as a shield for self-interested managerial acts: "These laws thereby give managers a long list of excuses for doing anything they like, even if it winds up harming the corporation, as long as they can make a plausible argument that their actions are intended to benefit some constituency group."²⁴⁶ Thus, workers' rights advocates share the concern shareholder supremacy supporters have regarding the potential use of other constituency statutes as a shelter from liability for self-interested managerial decisions.²⁴⁷

Beyond sharing shareholder supremacy supporters' concern with managers' potential, self-interested manipulation of other constituency statutes, workers' rights advocates also oppose these statutes because they do not impose any enforceable duties on managers and directors.²⁴⁸ These advocates contend that the lack of enforceable duties not only immunizes directors and managers from accountability, but provides no incentive to further the interests of workers.²⁴⁹ The permissive nature of the statutes, lacking enforcement through a private right of action, renders them ineffective as a guarantor of worker interests in corporation decision-making.²⁵⁰ Thus, other constituency statutes provide no incentive to directors and managers to consider worker interests because they cannot be held legally accountable for failing to do so.²⁵¹

Moreover, even when management may otherwise wish to consider worker interests in decision-making, management's exemption from legal liability for failing to do so, when contrasted with its potentially enormous legal liability for violating enforceable obligations owed to shareholders, may effectively preclude any consideration of worker interests.²⁵² Managers simply have no reason voluntarily to consider worker interests if doing so carries the risk of violating enforceable duties to shareholders but failing to do so bears no consequences.²⁵³ Therefore, even if other constituency statutes do not burden corporate management with the impossible task of owing fiduciary obligations to two potentially conflicting stakeholder groups, they are imprudent because they may shield self-interested managerial decisions from liability and because their

²⁴³ *Id.*

²⁴⁴ *See id.*

²⁴⁵ *See* Singer, *supra* note 11, at 499-501 (noting arguments by workers rights advocates against interpreting other constituency statutes as simply expanding managers discretion).

²⁴⁶ *Id.* at 500.

²⁴⁷ *See id.*

²⁴⁸ *Id.* at 501.

²⁴⁹ *Id.*

²⁵⁰ *Id.*

²⁵¹ *Id.*

²⁵² *See id.*

²⁵³ *See id.*

permissive nature does not provide management with any incentive to consider worker interests.

If other constituency statutes suffer from not going far enough in protecting worker interests due to their unenforceability, then it follows that a more drastic and effective system of fiduciary obligations is required.²⁵⁴ Yet an absolute extension of fiduciary protections to workers has faced opposition in light of both the allegedly impossible task of serving two masters²⁵⁵ and the shield such an extension affords self-interested managerial decisions.²⁵⁶ It is not surprising, therefore, that after comparing numerous definitions of fiduciary duty, such as a duty to pursue shareholder interests conditioned upon “consideration” of worker interests or conditioned upon acting in “good faith” towards other constituents, Jeffrey MacIntosh’s quest for a workable alternative fiduciary law ends by observing: “The main difficulty arises in finding an alternative that is both intellectually coherent and enforceable at reasonable cost, and that will not allow managers freedom to escape their responsibilities.”²⁵⁷

C. Reanalysis of an Absolute Extension of Fiduciary Duties to Workers in Light of the Actual Meaning and Function of Fiduciary Duties

The feasibility of an intellectually coherent and cost-justified corporate governance system that extends fiduciary protection to workers lies in recognizing fiduciary duties’ actual meaning and function.²⁵⁸ Fiduciary duties do not mandate a specific substantive outcome that boards must reach in pursuit of a certain group’s interests, but rather they require boards to procedurally conduct themselves in a certain way.²⁵⁹ The duty of care requires boards to inform themselves of pertinent facts,

²⁵⁴ *Id.*

²⁵⁵ See The Committee on Corporate Law, *supra* note 182, at 2269 (arguing that requiring directors to consider the various interests of numerous constituencies will transform an already difficult task of acting in the corporation’s and shareholders’ best interest into a harmful balancing act between interests).

²⁵⁶ See *supra* notes 242-247 and accompanying text.

²⁵⁷ MacIntosh, *supra* note 228, at 473.

²⁵⁸ Greenfield, *supra* note 28, at 238-39.

²⁵⁹ *Brehm v. Eisner*, 746 A.2d 244, 264 (Del. 2000). In *Brehm*, in characterizing the duty of care standard as a procedural obligation and not a duty requiring a particular substantive outcome, the Delaware Supreme Court stated:

As for the plaintiffs’ contention that the directors failed to exercise “substantive due care,” we should note that such a concept is foreign to the business judgment rule. Courts do not measure, weigh or quantify directors’ judgments. We do not even decide if they are reasonable in this context. Due care in the decisionmaking context is *process* due care only. Irrationality is the outer limit of the business judgment rule.

Id. (internal citations omitted) (emphasis in original); see also *In re Caremark International Inc. Derivative Litigation*, 698 A.2d 959, 967 (Del. Ch. 1996). The *Caremark* court stated:

[A] director’s duty of care can never appropriately be judicially determined by reference to the content of the board decision that leads to a corporate loss, apart from consideration of the good faith or rationality of the process employed. That is, whether a judge or jury considering the matter after the fact, believes a decision substantively wrong, or degrees of wrong extending through “stupid” to “egregious” or “irrational”, provides no ground for director liability, so long as the court determines that the process employed was either rational or employed in a *good faith* effort to advance corporate interests.

Id. (emphasis in original).

investigate various alternatives and outcomes, and sufficiently deliberate about a proposal before taking action.²⁶⁰ So long as these requirements are met, the business judgment rule protects directors from a breach of their duty of care and generally precludes judicial review of a deal's substantive terms.²⁶¹ Also, the foremost concern of corporate law's duty of loyalty is in regulating self-interested transactions between managers or directors and the corporation²⁶² through laws such as Delaware's requirement that directors and managers refrain from self-dealing, unless the transaction is approved by disinterested directors after full disclosure, disclosed to and approved by shareholders, or a court decides it is fair to the corporation.²⁶³ Thus, like the duty of care, the duty of loyalty mainly compels taking certain procedural steps before a board enters into a transaction involving self-dealing.²⁶⁴ Presumably, extending fiduciary protections to workers would afford them the same right shareholders have to approve the self-dealing transaction before it can be effected, but that right simply imposes an obligation on boards to obtain approval from both shareholders and workers. Surely this right, alone, does not create an impossible task in serving two masters, because it merely requires approval from two

²⁶⁰ See KLEIN & COFFEE, *supra* note 49, at 152-53 ("Under the majority formulation, any business judgment is immune from judicial review only if the directors first followed adequate procedures in reaching it.").

²⁶¹ *Kamin v. American Express Co.*, 383 N.Y.S.2d 807 (Sup. Ct. 1976), *aff'd*, 387 N.Y.S.2d 993 (App. Div. 1976). The Kamin court wrote:

The directors are entitled to exercise their honest business judgment on the information before them, and to act within their corporate powers. That they may be mistaken, that other courses of action might have differing consequences, or that their action might benefit some shareholders more than others present no basis for the superimposition of judicial judgment, so long as it appears that the directors have been acting in good faith.

Id. at 812.

²⁶² KLEIN & COFFEE, *supra* note 49, at 165.

²⁶³ DEL. GEN. CORP. LAW § 144.

²⁶⁴ For example, before a director can enter into a self-dealing transaction, most states require her to disclose her conflict of interest and obtain either shareholder or judicial approval of the transaction. See, e.g., DEL. GEN. CORP. LAW § 144. Some Delaware courts and a number of other states regard adherence to these statutes' procedures as eliminating the need for substantive judicial review and approve the transaction if it does not violate the business judgment rule or constitute waste. See *In re Wheelabrator Technologies Litigation*, 663 A.2d 1194, 1203 (Del. Ch. 1995) (holding that "Where there has been independent shareholder ratification of interested director actions, the objecting stockholder has the burden of showing that no person of ordinary sound business judgment would say that the consideration received for the options was a fair exchange for the options granted."); See *Puma v. Marriott*, 283 A.2d 693 (Del. Ch. 1971); See *Aronoff v. Albanese*, 446 N.Y.S.2d 368, 371-2 (App. Div. 1982). But see *Marciano v. Nakash*, 535 A.2d 400 (1987) (holding that although courts will approve of self-interested transactions ratified, after full disclosure, by disinterested directors or shareholders, if an independent board committee is unavailable or the shareholders are in a deadlock, courts must apply the "entire fairness" test."). Directors in some other states, however, who follow the procedural requirements for self-dealing transactions only shift the burden of proof to the plaintiff to prove that the transaction was clearly unfair. *Remillard Brick Co. v. Remillard-Dandini Co.*, 241 P.2d 66, 74-75 (Cal. Dist. Ct. App. 1952). However, as indicated by Delaware courts who use the comparably stringent requirements for lawful self-dealing by *controlling shareholders* (who owe minority shareholders fiduciary duties) by applying the seemingly substantive "entire fairness" test instead of the business judgment rule after evidence of informed, disinterested shareholder or board approval, even careful judicial analysis of "entire fairness" centers on closely scrutinizing the facts on record to assess the effectiveness of the board or shareholders' approval of the self-dealing transaction. See *Kahn v. Lynch Communication Systems*, 638 A.2d 1110, 1120-21 (stating that board approval of a controlling shareholder's self-interested merger transaction does not satisfy the "entire fairness" test unless the board was "truly independent, fully informed, and had the freedom to negotiate at arm's length.").

groups and does not require engaging in a substantive transaction favoring one constituency over another. Thus, in a typical scenario where worker and shareholder interests conflict, as where workers prefer the firm to invest in a less risky venture than the one favored by shareholders, all a fiduciary obligation extending to both workers and shareholders does is require consideration of both groups' interests under the duty of care and abstention from self-dealing transactions unless approved by both groups. Such an extension of fiduciary duties does not mandate a particular substantive result. Therefore, it is not rendered unworkable by being accorded to two groups of stakeholders.

Also, an extension of fiduciary protections to workers is not likely to be unresponsive to worker interests due to managements' use of this extension as a shield because, unconstrained by the current dominance of shareholder supremacy in law, directors are likely to act fairly and equitably, and to consider worker interests in decision-making.²⁶⁵ A study by Kent Greenfield and Peter Kostant examined how the shareholder supremacy rule affects board decision making by conducting two rounds of ultimatum games.²⁶⁶ In the first round, in negotiating deals, proposers and respondents acted for themselves, bargaining based on whatever factors were important to them.²⁶⁷ In the second round, the proposers had an obligation to act as an agent to a third party, thereby acting to maximize the return to that third party.²⁶⁸ Greenfield summarizes the outcome: "When proposers acted for themselves, they offered amounts to respondents in the range consistent with other experiments. But when they acted as an agent, trying to maximize the return to a third party, their willingness to share decreased significantly."²⁶⁹ The study suggests that, in the absence of shareholder supremacy, boards would consider worker interests in decision making in an effort to act fairly.²⁷⁰ In fact, this suggestion is buttressed by reviewing the effect of anti-takeover statutes passed in the 1980s.²⁷¹ Although the anti-takeover statutes granted greater discretion to managerial decisions by allowing some acts designed to thwart hostile takeovers, these statutes actually benefited workers by increasing wages one to two percent because the statutes alleviated fears of legal liability arising from shareholder discontent and thereby permitted boards to weigh worker interests more heavily than possible before the anti-takeover statutes.²⁷² Therefore, given boards' likely willingness to make fair and equitable decisions when unimpeded by the law, opponents of extending fiduciary protections to workers are mistaken in assuming that granting these protections to workers will merely shield self-interested managerial decision making and prove ineffective as a tool to protect worker interests.²⁷³ Rather, the likely outcome seems to be that requiring boards to owe fiduciary

²⁶⁵ Greenfield, *supra* note 28, at 179-80 (arguing that "Loosened from their legal duty to look after the interest of shareholders only, directors and managers would be able to allocate the corporate surplus with an eye to principles of fairness, equity, and just desserts, all of which they area legally prohibited from considering now.").

²⁶⁶ *Id.* at 176-78.

²⁶⁷ *Id.*

²⁶⁸ *Id.*

²⁶⁹ *Id.* at 177.

²⁷⁰ Greenfield, *supra* note 28, at 177.

²⁷¹ Marianne Bertrand & Sendhil Mullainathan, *Is There Discretion in Wage Setting? A Test Using Takeover Legislation*, 30 RAND J. ECON. 535 (1999).

²⁷² *Id.*

²⁷³ See Greenfield, *supra* note 28, at 179-80.

obligations to workers will provide boards with the necessary legal sanction to effectively consider interests that they are otherwise predisposed to consider.²⁷⁴

Moreover, even in cases where managements would seek to use their dual fiduciary obligations to shelter their self-interested decisions from legal liability, the technical enforcement of this dual fiduciary obligation will not allow managements to justify decisions that violate obligations towards one group merely because they meet obligations to another group.²⁷⁵ Managements' dual fiduciary duties require them to act in accordance to their duties to both shareholders and workers, not just one or the other.²⁷⁶ Thus, violating the duty of care owed to shareholders by not considering shareholder interests in a given corporate decision is not protected simply because management did consider worker interests.²⁷⁷

Similarly, in the context of the duty of loyalty, the law's general proscription of self-dealing is not weakened by owing this duty to both shareholders and workers.²⁷⁸ Whether a director steals from shareholders or both shareholders and workers, the director has breached his duty of loyalty; extending the duty of loyalty's general ban on self-dealing to workers does not make the director's theft more defensible.²⁷⁹ On the contrary, such an extension would make it harder for managers and directors to self-deal, because more corporate stakeholders would be monitoring board and management actions.²⁸⁰ Thus, even when the extension of fiduciary protections to workers does not prompt managements to act fairly towards workers, and instead triggers self-interested managerial decision making under the guise of furthering some stakeholder interest, such self-interested decisions will not be protected if they violate the fiduciary duties owed to either shareholders or workers.²⁸¹

D. Costs and Benefits of an Absolute Extension of Fiduciary Duties to Workers

²⁷⁴ See *id.*

²⁷⁵ Arguing that owing more than one stakeholder group will not shield managements' self-interested decisions, Greenfield states:

The only way that having more and broader responsibilities would make it easier for managers to avoid responsibility is that they could use one obligation as a defense to a claim that they failed at meeting another. But this is not a function of the number and scope of responsibilities but how they are *enforced*, and corporate law duties are simply not enforced in a way that would allow managers to play one duty off the other.

Id. at 139.

²⁷⁶ *Id.*

²⁷⁷ *Id.* (stating "No manager would be able to erect a defense to a shareholder claim by saying she was unable to pay attention to the impact of the decision on shareholders because she was thinking at the time about workers. The managers would have to do *both*.").

²⁷⁸ Greenfield, *supra* note 28, at 139.

²⁷⁹ *Id.*

²⁸⁰ Arguing that extending protection of managers' fiduciary duties to nonshareholding stakeholders will not only avert weakening fiduciary obligations, but rather actually help prevent self-dealing, Greenfield states:

In corporate law, loyalty requires managers not to engage in self-dealing. Such an obligation would not be weakened at all by including workers among the beneficiaries of managers' fiduciary duties. Rather, adding to the number of people who benefit from managers' fiduciary duties will make it *more* difficult for managers to self-deal. More corporate stakeholders will have an interest in monitoring managerial conflicts of interest.

Id.

²⁸¹ *Id.*

Regardless of the large disparity between shareholder supremacy supporters' estimated high cost of a system extending fiduciary protections to workers and the actual low cost of the system demonstrated above, to warrant adoption, such a system must provide benefits sufficient to justify bearing even minimal costs. To be certain, this corporate governance system bears efficiency costs--increased boardroom deliberation and tension combined with a lack of certainty regarding the amount of consideration the respective interests of workers and shareholders are to be given impede efficient decision making.²⁸² The system also bears financial costs,²⁸³ such as expenses required to obtain advice about worker interests,²⁸⁴ loss of shareholders' capital contributions due to a decreased ability to monitor management,²⁸⁵ and a potential increase in corporate resources diverted to defending costly litigation.²⁸⁶ Also, the uncertainty a new, more complicated fiduciary law presents²⁸⁷ may deter investment of capital. Thus, the analysis concerning the desirability of a system of corporate governance that grants workers fiduciary protections narrows down to an assessment of whether the system's benefits outweigh its costs.²⁸⁸

Insofar as the historic neglect of worker interests in major corporate decision making has inflicted social harms such as high unemployment rates, a widening gap between rich and poor, increased demand for public welfare assistance, and untreated medical illnesses,²⁸⁹ certainly a corporate governance system that considers workers' well being will produce the benefit of reducing these harms.²⁹⁰ As stated above, this does not saddle directors with the impossible task of both closing a plant in accordance with shareholder wishes and keeping a plant open to satisfy workers.²⁹¹ Rather, workers' fiduciary protections compel consideration of worker interests in decision making and, even if directors ultimately decide to shut the plant down, this duty would require them to provide the displaced workers with appropriate relief such as adequate severance

²⁸² See MacIntosh, *supra* note 228, at 444 (arguing that the uncertainty of requiring management to both maximize shareholder wealth and consider other interests, in part, makes this consideration standard "fundamentally incoherent").

²⁸³ Greenfield, *supra* note 28, at 239-40.

²⁸⁴ *Id.* (stating "[i]ndeed, as boards of directors typically include strong advocates of shareholders interests, perhaps boards who ascribe to a more robust conception of fiduciary duty doctrine would find it useful to invite representatives of other stakeholders to be among their members To the extent that this new version of fiduciary duty imposes more difficult obligations, the cost of monitoring the behavior of directors will likely increase.").

²⁸⁵ *Id.* at 38 (stating "[p]erhaps a loosening of management's fiduciary duty to shareholders will make shareholders less likely to invest, because they will lose some of their legal power to monitor and constrain management.").

²⁸⁶ See The Committee on Corporate Laws, *supra* note 182, at 2270 (stating "[i]f directors have, or may have, recognized legal duties to other constituencies, perhaps a new class or classes of plaintiffs will have access to the courts to redress perceived breaches of those duties or to challenge directors' failures to take various competing interests into account.").

²⁸⁷ See MacIntosh, *supra* note 228, at 445 ("The intellectual incoherency of the standard creates great uncertainty about how judges will apply it.").

²⁸⁸ O'Connor, *supra* note 4, at 1259.

²⁸⁹ See *supra* notes 4-14 and accompanying text.

²⁹⁰ See O'Connor, *supra* note 4, at 1197-98 (asserting a relationship between management decisions and resulting work wellbeing).

²⁹¹ See *supra* Part II.B.

payments and job retraining.²⁹² Therefore, even if granting workers fiduciary protections does not always require the substantive result that they keep their jobs, at the very least it does help minimize the unjustifiable social costs caused by a total neglect of worker interests.

Moreover, the unpredictable dependence of workers' jobs on a decision-making process that excludes consideration of their interests has contributed to the underperformance of U.S. businesses internationally.²⁹³ Corporate law's exclusive concern with shareholder interests has sanctioned corporate decisions and acts that have stripped workers of job security.²⁹⁴ Companies with low-margin operations have cut jobs to lower labor costs and increase profit.²⁹⁵ Leveraged buyouts significantly increase the debt of the acquired company, leading to massive layoffs.²⁹⁶ The resulting loss of job security has reduced workers' incentives to increase productivity.²⁹⁷ Also, along with the cost of stagnant productivity, workers' substandard work effort imposes additional monitoring costs.²⁹⁸ The disincentive that a lack of job security fosters results in work performance that barely meets minimum standards,²⁹⁹ requiring employers to incur high monitoring costs to avoid shirking.³⁰⁰ Therefore, decision making focused solely on shareholder interests has contributed to a national economy with underperforming businesses plagued by stagnant productivity and high monitoring costs.³⁰¹

By imposing on directors an enforceable obligation to consider worker interests in boardroom deliberations, extending fiduciary protections to workers will help assure job security and, consequently, contribute to increased productivity.³⁰² When workers are assured that the corporate decision-making process includes consideration of their interests, they are induced to work harder and more efficiently, confident that their hard work will not result in a board's exclusively profit-driven decision to strip them of their jobs.³⁰³ Indeed, as Marleen O'Connor notes, productivity is likely to be higher in job markets where dedicated, long-term employees are offered incentives to maximize production through job security, higher wages, and seniority benefits than in markets where productivity relies on extensive monitoring and the negative and discouraging

²⁹² O'Connor, *supra* note 4, at 1194.

²⁹³ Singer, *supra* note 11, at 508-09.

²⁹⁴ O'Connor, *supra* note 4, at 1196-7.

²⁹⁵ *Id.* at 1196.

²⁹⁶ *Id.* at 1201.

²⁹⁷ Singer, *supra* note 11, at 509.

²⁹⁸ O'Connor, *supra* note 46, at 908.

²⁹⁹ See *id.* at 918-23. O'Connor explains that maximum worker productivity depends on workers' trust in management that managers will not engage in opportunistic behavior and renege on implicit employment agreements concerning job security and workplace conditions. However, when the labor market becomes volatile, the security of these long-term employment agreements is jeopardized because workers risk job loss due to plant closings, layoffs, acquisitions, or bankruptcy and fear opportunistic behavior by managers in withholding implied benefits such as severance pay and pay increases based on seniority. This mistrust creates a "prisoner's dilemma" in which workers are tempted to withhold their work effort fearing imminent job loss and managers are tempted not to make commitments concerning job security as it may cause employees to shirk. As such, the lack of cooperation between managers and workers that results from this prisoner's dilemma poses a major obstacle to optimizing worker performance and production. *Id.*

³⁰⁰ *Id.*

³⁰¹ Singer, *supra* note 11, at 508-09.

³⁰² *Id.*

³⁰³ *Id.*

work environment this monitoring creates.³⁰⁴ Thus, extension of fiduciary protections will help workers attain the job security required to foster increased productivity and a stronger economy.³⁰⁵

In addition, although owing an additional stakeholder group enforceable fiduciary duties can be deemed a cost due to the likely increase in litigation, it can also be regarded as serving an important social role by enlarging the group of persons who oversee executive behavior.³⁰⁶ In corporate proxy contests, managements of publicly held corporations rarely lose, indicating a lack of adequate oversight by shareholders.³⁰⁷ A number of factors explain managements' likely success in proxy contests.³⁰⁸ First, whereas managements can generally use corporate funds to finance expensive proxy contests, shareholders usually need to incur these high costs themselves.³⁰⁹ Moreover, in light of portfolio diversification, which allows shareholders to nearly eliminate the risk of investing in a poorly managed company, shareholders do not have the incentive to expend money, time, and attention to proxy contests.³¹⁰ Finally, a shareholder has a further disincentive to spend time and money on waging a proxy contest because doing so would gratuitously create a value for all shareholders even though only she bore the costs.³¹¹ Thus, even though these factors explain shareholder passivity, they also reveal the need for greater oversight of executive behavior.³¹²

In granting another group of stakeholders beneficiary status, extending fiduciary obligations to workers would help fill the void in executive oversight by allowing workers to hold directors and managers liable for their unlawful acts.³¹³ Indeed, as Marleen O'Connor observes, "[e]mployees are uniquely situated to review executive inefficiency and self-serving behavior."³¹⁴ Through their associating with the company on a daily basis, workers experience the product of their work and skill, observe inventory levels, witness managers' dispositions, and partake in company gossip.³¹⁵ Besides observing executive decision making from a unique vantage point, workers are much more willing to challenge board decisions and actions than shareholders, because management decisions affect them more.³¹⁶ Since workers' investment in the firm is much more firm-specific and less transferable than shareholder investments, unsatisfied workers, unlike shareholders, cannot simply either sell their investments in a liquid market or avoid the impact of bad management by portfolio diversification.³¹⁷ For a worker to "sell her investment," she must quit and risk detrimental financial consequences.³¹⁸ Therefore, due to the unique perspective workers have regarding

³⁰⁴ O'Connor, *supra* note 46, at 908.

³⁰⁵ *See id.*

³⁰⁶ *See* O'Connor, *supra* note 4, at 1252.

³⁰⁷ KLEIN & COFFEE, *supra* note 49, at 179.

³⁰⁸ *Id.*

³⁰⁹ *Id.*

³¹⁰ *Id.*

³¹¹ *Id.*

³¹² *See* KLEIN & COFFEE, *supra* note 49, at 179.

³¹³ O'Connor, *supra* note 4, at 1255.

³¹⁴ *Id.*

³¹⁵ Greenfield, *supra* note 15, at 301.

³¹⁶ *See id.* at 302.

³¹⁷ *Id.*

³¹⁸ *Id.*

executive conduct and their added incentive to challenge such behavior, extending fiduciary protections to workers produces the socially beneficial outcome of an increase in the level and effectiveness of executive behavior oversight. Moreover, in light of the potential benefits conferred by a corporate governance system that extends fiduciary protections to workers—including reduced unemployment, decreased reliance on public assistance, increased job security, increased productivity, decreased monitoring costs for U.S. businesses, and more effective oversight of corporate misbehavior—the relatively minimal efficiency and financial costs it may create are certainly worth incurring.

CONCLUSION

Under the current formulation of corporate law, directors and managers owe the fiduciary duties of care and loyalty to shareholders only. Although advocates of this shareholder supremacy rule justify limiting fiduciary protections to shareholders based on a number of theories, such as property, agency, residual claimant, and contracting problems, these rationales generally either overlook workers' stakeholder interests or rest on inaccurate notions of corporate terminology.

Notwithstanding the flawed arguments for restricting fiduciary duties to shareholders, the advisability of extending workers these protections would also depend on its feasibility, namely its likely effects and drawbacks. First, supporters of shareholder supremacy argue that extending fiduciary protections to workers is unfeasible because worker interests are too heterogeneous to owe all workers the same fiduciary duty. However, just as a common goal of profit maximization has led to different classes of stock being successfully protected by the same fiduciary duties, it is likely that workers' shared interests in job security, safe working conditions, and fair wages will also allow them to feasibly be protected by fiduciary duties extended to them as a group. Second, shareholder supremacy supporters contend that, in light of the divergent interests between shareholders and workers, directors cannot owe fiduciary duties to both groups. Yet this argument is overstated both because directors have always owed fiduciary duties to different classes of stock, with often opposing interests, and because workers and shareholders share more interests than typically postulated. In addition to the inability of the latter two arguments to cast doubt on the feasibility of according workers fiduciary protections, the viability of a system affording workers greater protections is shown by the success met by both the German and Japanese corporate governance systems. Although both systems' relatively broad grant of worker protections carries certain economic sacrifices, at the very least, the systems prove that a corporate governance regime that affords workers substantial protections is both feasible and workable.

Although effectively countering potential drawbacks to a system that extends fiduciary protections to workers establishes that such a system may be feasible, a particular fiduciary law's likely effects, costs, and benefits also must be assessed before conclusively recommending it. A corporate governance system that grants workers broader protections might include either a fiduciary law that compels directors to owe workers fiduciary duties or a law that permits directors to consider worker interests in decision making. Both the absolute and permissive fiduciary laws may arguably serve as a shield for management decisions. However, as statistical evidence and experimental tests indicate, when the law permits management to consider worker interests, it is likely

to do so. Yet, a permissive fiduciary law is rightly accused of not going far enough in protecting worker interests by merely giving directors discretion to consider their interests. Thus, an absolute fiduciary law is the preferable alternative by forcing directors to consider workers' interests.

Nevertheless, even an absolute fiduciary law may be deemed flawed if it burdens management with the impossible task of serving "too many masters." The supposed flaw fails to undermine an absolute fiduciary duty, however, because it misconstrues the meaning and function of the fiduciary duty. Once the fiduciary duty is understood not to compel particular substantive decisions by the board, but rather require that the board take certain procedural steps, it is clear that the "too many masters" argument does not make an absolute fiduciary law unworkable.

Finally, to justify implementing this absolute fiduciary law, its benefits must outweigh costs. A law requiring directors to owe workers fiduciary duties carries the potential costs of increased boardroom tension and deliberation, lack of certainty, and costly litigation. In spite of such costs, if the benefits of such a law outweigh them, the law should be adopted. A non-exhaustive list of possible benefits of an absolute fiduciary law include lowering unemployment, decreasing reliance on public assistance, providing medical treatment to discharged employees, increasing U.S. business's productivity and lowering monitoring costs, and ensuring more aggressive oversight of executive behavior. Given the magnitude of such benefits, especially relative to costs, a law that extends fiduciary protections to workers should be adopted.